Lectures on

COMPANY LAW

[Companies Act, 2013]

By

Prof. Dr. Rega Surya Rao

Principal

P.D.Ps Law College (AIDED)

PHALTAN Dist., Satara, Maharashtra

Formerly

Lecturer in Law

SIR C.R. REDDY LAW COLLEGE, Eluru, A.P.

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Lectures on Company Law

Lecture - I
INTRODUCTION

This Lecture deals with –

I. The Companies Act, 1956 (Old Act)

1. Introduction.
2. Historical Background.
3. Changes brought about by the Companies Act, 1956.
4. Amendments to the Companies Act, 1956 and
5. Salient Features of the Companies (Amendment) Act, 1988.

II. The Companies Act, 2013 (The New Act)

1. Introduction.
2. Historical Background.
3. Changes Brought about by the New Act, 2013.
4. New Provisions introduced under the Act, 2013 and
5. Provisions under the Old Act, 1956 discarded/ deleted by the New Act, 2013.

I. The Companies Act, 1956 (The Old Act)

1. Introduction: The Law relating to Companies in India is governed by the Companies Act, 1956. It was passed in 1956 and came into force on 01.04.1956. It extends to the whole of India. It applies to the State of Nagaland subject to such modifications as the Central Government may by notification in the official gazette specify. It has been amended several times i.e. 1960, 1962, 1963,

1964, 1965, 1966, 1967, 1969, 1974, 1977, 1985, 1988, 1996, 1999, 2000, 2001, 2002 (as amended by the Companies (Amendment) Act, 2002 and Companies (Second Amendment Act, 2002). The last amendment i.e. prior to the passing of the Companies Act, 2013 was made in 2002 (Act 11 of 2003). The Monopolies and Restrictive Trade Practices (Amendment) Act, 1984, which was passed to amend the M.R.T.P.Act, 1969 also amended some sections and omitted some sections (Cl.(18.A) of Sec.2 and explanation there to Ss.108.A – 108.H) and Schedule XIII of The Companies Act, 1956. It is a mammoth legislation containing 658 sections divided into 13 parts and 15 Schedules.

Part I containing Sec.1-10D deals with preliminary aspects. Part I.A containing Sections 10.E, 10.F and 10.FA deals with Board of Company Law Administration. Part I.B containing Sections 10.FB, 10.FC, 10.FD, 10.FE, 10.FF, 10 FG, 10.FH, 10.FI, 10.FJ, 10.FK, 10.FL, 10.FM, 10.FN, 10.FO and 10.FP made provisions for constitution/establishment of National Company Law Tribunal. Part I.C containing Sections 10.FQ-10.FZ, 10.FZA, 10.G and 10.GA-10.GF provides for Appellate Tribunal. Part II containing Sections 11 to 54 deals with 'Incorporation of Company and matters incidental thereto'. Part III containing Sections 55 to 81 lays down the provisions relating to 'Prospectus and Allotment and other matters relating to issue of Shares or Debentures'. Part IV containing Sections 82 to 123 deals with 'Share Capital and Debentures'. Part V containing Sections 124 to 145 provides for 'Registration of Charges'. Part VI containing Sections 146 to 424 divided in to 8 chapters lays down various provisions relating to the Management and Administration of the Companies. Part VI.A containing Sections 424.A to 424.L provides for 'Revival and Rehabilitation of sick Industrial Companies.'

Part VII containing Sections 425 to 560 divided into 5 Chapters deals with winding up of the company. Part VIII containing Sections 561 to 564 relates to application of the Act to companies formed or registered under the previous Companies' laws. Part IX containing

Sections 565 to 581 speaks about the companies authorised to register under the Companies Act, 1956. Part XI.A containing Sections 581.A to 581.Z, 581.ZA to 581.ZT divided in to 12 Chapters lays down various provisions relating to Producer Companies. Part X containing Sections 582 to 590 lays down the provisions relating to winding up of unregistered companies. Part XI containing Sections 591 to 608 lays down the provisions relating to establishment of Foreign Companies i.e. Companies incorporated outside India and having the plan of business in India (E.g.: Union Corbide Corporation, U.S., and Union Corbide Corporation India Limited, Bhopal). Part XII containing Sections 609 to 614.A deals with Registration Offices, Officers and Fees. Part XIII containing Sections 615 to 658 lays down the general provisions relating to power of the Central Government over Companies, application of the Act to the Government Companies, special provisions as to the companies established in the State of Jammu & Kashmir, Offences, Legal Proceedings etc.

In addition to the above, Schedule I contains Table A to Table F. Table A contains regulations for management of a Company limited by shares. Table B contains Memorandum of Association of a Company limited by shares. Table C contains Memorandum and Articles of Association of a Company limited by guarantee not having a share capital and Table D refers to such company having a share capital. Table E contains Memorandum and Articles of Association of an unlimited company. Table F contains Form of Statement to be published by limited Banking Companies, Insurance Companies and deposit, provident or benefit societies. Schedule 1. A contains list of relatives. Schedule II consisting of 3 parts contains the matters to be specified in prospectus and reports to be set out therein. Schedule III consists of 3 parts. It provides for form of statement in lien of prospectus to be delivered to the Registrar of a Joint Stock Companies by a Company, which does not go to allotment on a prospectus issued and reports to be setout therein. Schedule IV also contains 3 parts. It provides for form of statement in lien of

prospectus to be delivered to Registrar by a private company on becoming a public company and reports to be set out therein. Schedule V divided in to two parts contains Contents and Form of Annual Return of a Company having a share capital. Schedule VI consisting of 4 parts contains form of Balance Sheet, Requirements as to Profit and Loss Account etc. Schedule VII contains Restrictions on Powers of Managing Agents/Secretaries and Treasurers. Schedule VII contains Restrictions on powers of Managing Agents/ Secretaries and Treasurers. Schedule VIII consisting of Declarations to be made by firms, private companies and other bodies corporate acting as Managing Agents/Secretaries and Treasurers. Schedule IX contains of Form of Proxy. Schedule X contains of Table of Fees to be paid to the Registrar. Schedule XI consists of Form in which Sections 539 to 544 of Act are to apply to cases where an application is made under Section 397 or 398. Schedule XII contains Enactment Repealed. Schedule XIV contains Rates of Depreciation and Schedule XV refers to Arms and ammunition and allied items of defence equipment.

2. Historical Background

The institution of joint stock companies for trading and other purposes in England dates back to several centuries. In England, the right to trade with limited liability was granted for the first time by passing of the Limited Liability Act, 1855. It remained in force for a few months and was repealed by the Joint Stock Companies Act, 1856.

In India, an Act entitled 'Registration of Joint Stock Companies Act', was passed for the first time in 1850 for registration of joint stock companies. It was based on the English Companies Act of 1844. It made provisions for formation and management of joint stock companies and did not confer the privilege of limited liability of the members. In 1857, an Act for incorporation and regulation of Joint Stock Companies and other Associations was passed. It conferred on members limited liability. However, the privilege of limited liability was not extended to banking or insurance companies.

Act VII of 1860 passed on the lines of the English Act of 1857 removed this disability. Later, a Comprehensive Act was passed in India in 1866 on the lines of English Act of 1862. It consolidated and amended the laws relating to the incorporation, regulation and winding up of the companies and other associations. The Act of 1866 was recast in 1882 and further amending Acts were passed till the passing of the Act VII of 1913. It was amended several times during 1913-1946 and was ultimately repealed by the present Companies Act, 1956. It was enacted on the lines of the English Act of 1948. The Companies Act, 1956 is a consolidated Act and not an amending Act. It was brought under the recommendations of H.C.Bhaba Committee. It is a largest piece of legislation containing 658 Sections and 15 Schedules ever passed by the Indian Parliament. It aims to achieve the socialistic pattern of the society as enshrined in our constitution.

The Companies Act, 1956 is subject to criticism on the grounds that

i) It has been amended several times i.e. in 1960, 1962, 1963, 1964, 1965, 1966, 1967, 1969, 1974, 1977, 1985, 1988, 1996, 1999, 2000, 2002 (as amended by the Companies (Second Amendment) Act, 2002). The Monopolies and Restrictive Trade Practice (Amendment) Act, 1984, which was passed to amend the M.R.T.P.Act, 1969 also amended some sections and omitted some sections (Clause 18(A) of Section 2 and explanation thereto, Ss.108.A-108.H) and Schedule XIII of the Companies Act, 1956.

ii) It is not suitable to the needs of the people in India.

iii) The Supreme Court several times opined that the present Companies Act is out dated and should be reformed.

3. Changes brought about by the Companies Act, 1956:

Following are the major changes brought about by the Companies Act, 1956.

i. The Central Government has been empowered to compel any company to change its name wherever the existing name is considered to be undesirable by it (Central Government) (Sec.20).

ii. All Private Limited Companies shall have to use the words 'Private Limited' compulsorily as the last word of their name (Sec.13).

iii. All investments made by a company on its own behalf shall have to be made and held by it on its own behalf and where any such investments are not so held at the commencement of the Act, the company shall, within a period of one year from such commencement, either cause them to be transferred to and hold them, in its own name, or dispose of them (Sec.49).

iv. Only two types of share capital viz. equity share capital and preference share capital has been recognized (Sec.86).

v. If the company refuses to effect transfer of shares, the transferor or transferee, as the case may be, has been given a statutory right to appeal to Central Government against such refusal to register the transfer (Sec.111).

vi. A Company can not issue any debenture carrying voting rights at any meetings of the company, whether generally or in respect of particular classes of business. (Sec117).

vii. The total managerial remunerations payable by a public company to its Directors and its Managing agents, Secretaries and Treasurers or Manager in respect of any financial year cannot exceed eleven percent of the net profits of the company (Sec.198).

viii. Strict restrictions have been imposed on the relatives of Directors to hold office of profit or being appointed as directors etc. in the same company (Sec.314).

ix. One person cannot be a Director of more than 20 companies

at one time. Likewise, a Managing Director cannot be appointed for a term exceeding five years at a time.

x. The Central Government has been empowered to abolish the managing agencies and secretaries and treasurers and in Section 324.A, it has been provided that no company shall appoint or reappoint any managing agent and secretaries and treasurers on or after the 3rd day of April 1970.

xi. The shareholder has been given statutory right to institute suits in the Court, if the Company's management is being conducted in a manner prejudicial to public interest or to company or where the affairs of the company are being conducted in a manner oppressive to such member or members (Sections 397 & 398).

xii. The Central Government has been empowered to constitute an Advisory Committee consisting of not more than five persons with suitable qualification for the purpose of advising it and the Company Law Board on such matters arising out of the Administration of the Act as may be referred to it.

4. Amendments to the Companies Act, 1956

The Companies Act, 1956 has been amended several times since it was codified. The provisions of these Amending Acts have been incorporated in the Book at appropriate places.

Monopolies and Restrictive Trade Practice (Amendment) Act, 1984:— It has been passed to amend the M.R.T.P. Act, 1969 and the Companies Act, 1956. The

following Sections and Schedule of the Companies Act have been omitted by this Amending Act:

1. Clause (18.A) of Sec.2 and the explanation thereto.
2. Sections 108.A to 108.H.
3. Schedule XIII.

This Amending Act has introduced many amendments in the M.R.T.P.Act, 1969. Some of these amendments are also relevant with reference to the Companies Act.

Companies (Amendment) Act, 1985: It has substituted a new section for Section 293.A and inserted a new Section 529.A. It has amended Sections 396, 529 and 530.

The Companies (Amendment) Act, 1988: It has introduced many amendments in the Companies Act. The power of the Company Law Board has been increased. Section 10.E has been amended and a new Section 10.F has been inserted. These amendments seek to provide for the constitution of a Company Law Board, which will exercise, and discharge powers and functions conferred on the Board. By this Act, several new Sections (E.g. 2(45.A)l, 10.E(1.A), 10.F, 58(3.A), 73(10), 80(5.A)l, 80.A, 130(1.A), 130(1.B), 130(1.c), 205(2.B), 206.A, 241(2)(dd), 247(1.A), 370, expl. 383.A(1.A), 462(4.A), 551.2.A), 619.A(4), 621.A, Schedule XIII, Schedule XIV, etc.) have been inserted and several sections (e.g. 2(45), 5, 10.E(1), 10.E(5)l, 111, 130(2), 205(2)(d), 209(3), 219(2), 233.B(2), 235, 248(1), 250(3), 250(4), 250(5), 269, 408(1), 408(2), 637(1), etc.) have been substituted. Besides, several sections (E.g. 33(2),

43, 43.A(8) (c), 58(3) (a), 73(1.A), 73(2), 73(2.A), 74, 108, 113(1), 113(3), 130(3), 161(1), 205.A(1), 217(2.A)(a), 219(4), 220(2), 236, 237, 250(5), 304(2)(b), 314(1)(b), 314(2.D), 408(5), 409, 634.A, 635(4), 637(2), 614(1) etc.) have been amended. Several Section (E.g. 43.A(6), 43.A(7), 155, 156, 250(6), 250(7), 637(2.A), etc.) have been omitted.

The Monopolies and Restrictive Trade Practices (Amendment) Act, 1991: By this Act Sections 108.A to 108.I have been inserted in the Companies Act. These Sections impose certain restrictions on the acquisition and transfer of shares of or by certain bodies corporate. Besides, a new Schedule XV has been inserted in the Companies Act.

The Depositories Act 1996: Certain provisions of the Companies Act have been amended and a few new sections have also been inserted by these Acts. They have been stated at the appropriate places in the Book.

The Companies (Amendment) Act, 1996: Sections 17, 18, 58.A, 80, 153.B, 370, 372 and 530 have been amended and a new Section 610.A has been inserted by this Act.

The Companies (Amendment) Act, 1999: Several sections of the Companies Act have been amended and several new sections have been inserted by this Act. They have been stated at the appropriate places in the Book.

The Companies (Amendment) Act, 2000: By this Act several sections have been amended and several new sections

have been inserted. It has amended Sections 2, 3, 4, 11, 16, 22, 25,39, 40, 43-A, 44, 49, 54, 56, 58-A, 59, 60, 63, 67, 68, 69, 70, 72, 73, 75, 76, 77, 79, 80, 80-A, 84, 89, 95, 97, 107, 108-I, 111, 113, 115, 118, 127, 133, 137, 142, 143, 144, 146 to 152, 153.A, 153.B, 154, 157 to 160, 162, 163, 165, 168, 176, 187.B, 187.C, 188, 192, 193, 196 to 199, 201 to 204, 205, 105.A, 209, 209.A, 210, 211, 212, 215, 217 to 221, 223, 224, 226, 227, 232 to 234.A, 239 to 243, 245, 247, 250 to 252, 269, 272, 274 to 277, 279, 283, 286, 292, 292.A, 294, 295, 299 to 305, 307 to 309, 314, 318, 320, 322, 323, 349, 350, 355, 370.A, 371, 374, 383.A, 387, 388.E, 391, 393 to 395, 398, 402, 404, 405, 407, 409, 416, 420, 423, 427, 445, 454, 469, 481, 485, 491, 494, 495 to 497, 500, 501, 508, 509, 513, 514, 516, 542, 543, 547, 550, 551, 559, 560, 568, 583, etc. It has inserted several new sections (E.g. 17.A, 55.A, 58.AA, 58.AAA, 60.A, 60.B, 68.Bl, 117.A, 117.C, 192.A, 292.AA, etc.) and omitted several existing sections (E.g. 88, 248, 249, 261, 298, 324, 324.A, 325l, 325.A, 326 to 348l, 351 to 354, 356 to 369l, 375, 375, 377 to 383 etc.)

The Companies (Amendment) Act, 2001: The Companies (Amendment) Act, 2001 has been passed to amend Sections 77.A and Sections 292. It has come into force on 23.10.2001.

The Companies (Amendment) Act, 2002: This Act has been passed so as to introduce a new Part IX.A (Sections 581.A to 581.ZT). The provisions of these Sections deal with the producer companies.

The Companies (Second Amendment) Act, 2002: By this Act several Sections have been amended and several new Sections

have been inserted in the Companies Act. The Company Law Board has been dissolved and its powers and functions have been conferred on the National Company Law Tribunal and the Central Government. Section 10.FB makes it clear that the Central Government shall, by notification in the Official Gazette constitute a Tribunal to be known as the National Company Law Tribunal to exercise and discharge such powers and functions as may be conferred on it by or under this Act or any other law for the time being in force. As per Section 10.FQ any person aggrieved by an order or decision of the Tribunal may prefer an appeal to the Appellate Tribunal and any person aggrieved by any decision or order of the Appellate Tribunal may file appeal to the Supreme Court. The provisions relating to the Tribunal, Appellate Tribunal, etc.

This Act has also inserted new Part VI.A consisting of Sections 424.A to 424.L dealing with the revival and rehabilitation of sick industrial companies.

Extent of the Companies Act, 1956: The Indian Companies Act came into force on the 1st April 1956 and it extends to the whole of India. It applies to the State of Nagaland subject to such modifications as the Central Government may, by notification in the Official Gazette, specify. In construing the Act it is permissible to refer to English case law on the subject. It is also notable that where the words in the Indian Companies Act are the same as in the English Statute, the English decisions can be referred to guide in their interpretations.

5. Salient Features of the Companies (Amendment) Act, 1988

The Companies (Amendment) Act, 1988 introduced drastic changes in the administration of companies in India. The salient features of the Act are detailed below:

i. The setting up of an independent Company Law Board, vested with such judicial and quasi-judicial powers as exercised by the Courts of law and the Central Government.

ii. Compounding of offences punishable with fine.

iii. Dispensing with Government approval for managerial appointments and remuneration subject to the fulfillment of certain statutory guidelines which are proposed to be incorporated in the Act itself.

iv. Delinking of the rates of depreciation from the rates specified under the Income-Tax Act and laying down the rates of depreciation in the Act itself to reflect the true and fair view of the state of affairs of the company.

v. Protecting the interests of the investors by providing for intervention by the Company Law Board against non-repayment of public deposits; compulsory redemption of preference shares in certain cases; requiring companies to disclose reasons for refusal to register transfer of shares; and protecting the rights of the transferee pending mutation of his name in the registers of members; and also compulsory listing of all public issues.

vi. Reducing unnecessary cost or burden by requiring companies to attach only an abridged form of prospectus to the application form and only an abridged version of balance sheets and auditors' report to members and also by requiring companies to hold a poll in a general meeting only at the instance of the shareholders having some minimum stake in the company; and further requiring companies to file full annual return only once in a six years.

vii. Provision for disclosure of information relating to conservation of energy, technology absorption, foreign exchange earnings and outgoing as well as particulars of employees having some minimum stake in the company and drawing remuneration in excess of that drawn by managerial personnel.

II. The Companies Act, 2013 (The New Act)

1. Introduction

Earlier i.e. prior to 2013, the law relating to companies was governed by the Companies Act, 1956. It was amended several times i.e. 25 times resulting in so many changes that were brought about and hence, the authorities felt necessary to pass a new Act repealing the Old Act of 1956. For the purpose, the Government of India introduced a new Company Law Bill, 2012 on 18-12-2012 and after the approval by the Lok Sabha, the Bill was introduced in the Rajya Sabha on 08-08-2013. After approval by the Rajya Sabha, the Bill received the assent of the President of India on 29-08-2013 and passed into law as "The Companies Act, 2013" (18 of 2013).

Now, the law relating to companies is governed by the Companies Act, 2013, which came into force on 29th August, 2013. The main object of the Act is to consolidate and amend the law relating to companies. It extended to the whole of India. Section 1 containing short title, extent, commencement and application shall come into force at once and the remaining provisions of the Act shall come into force on such date as the Central Government may by notification in the Official Gazette appoint and different dates may be appointed/fixed for different provisions of the Act. It contains 470 Sections divided into 29 Chapters and 7 Schedules (as against 658 Sections divided into 13 Parts and 15 Schedules of the Old Act i.e. The Companies Act, 1956).

Chapter I (Preliminary) contains two sections. Section I refers to short title, extent, commencement and application of the Act. Section 2 provides for various (95) definitions. Chapter II containing

Sections 3 to 22 provides for various provisions relating to 'Incorporation of Company' and matters incidental thereto. Chapter III containing Sections 23 to 42 deals with prospectus and prescribes procedure for allotment of securities. Chapter IV containing Sections 43 to 72 lays down the provisions relating to issue, subscription and allotment of shares (share capital) and debentures. Chapter V containing Sections 73 to 76 provides procedure for acceptance of deposits by companies. Chapter VI containing Sections 77 to 87 deals with Registration of Charges. Chapter VII containing Sections 88 to 122 lays down various provisions relating to Management and Administration. Chapter VIII containing Sections 123 to 127 contains the provisions relating to 'Declaration and Payment of Dividend'. Chapter IX containing Sections 128 to 138 contains the provisions relating to maintenance of books and accounts of the Companies. Chapter X containing Sections 139 to 148 provides for appointment of Auditors and Audit Procedure. Chapter XI (Sections 149 to 172) provides for various provisions relating to Board of Directors of the Companies viz. appointment of Directors, qualifications, removal, punishment etc. Chapter XII (Sections 173 to 195) deals with Meetings of the Board (of Directors) and its powers. Chapter XIII containing Sections 196 to 205 deals with Appointment and Remuneration of Managerial Personnel. Chapter XIV (Sections 206 to 229) lays down the procedure for Inspection, Inquiry and Investigation. Chapter XV containing Sections 230 to 240 provides for the provisions relating to Compromises, Arrangements and Amalgamations. Chapter XVI (Sections 241 to 246) deals with Prevention of Oppression and Mismanagement. Chapter XVII containing Section 247 envisages Valuation of properties of the companies by registered valuers. Chapter XVIII (Sections 248 to 252) lays down the provisions relating to removal of names of companies from the register of companies. Chapter XIX (Sections 253 to 269) provides for revival and rehabilitation of sick companies. Chapter XX (Sections 270 to 365) provides for various provisions relating to different modes of winding up namely i) winding up by Tribunal (Part I - Sections 271 to 303); ii) Voluntary winding up (Part II – Sections 304 to 323); iii) Common provisions

for every mode of winding up (Part III – Sections 324 to 358); iv) Provisions relating to appointment, powers, functions etc. of Official Liquidators (Part IV – Sections 359 to 365). Chapter XXI comprises of two parts – Part I containing Sections 366 to 374 makes provision for registration of companies authorized to register. Part II containing Sections 375 to 378 provides for the winding up of unregistered companies. Chapter XXII (Sections 379 to 393) lays down various provisions relating to companies incorporated outside India. Chapter XXIII (Sections 394 and 395) lays down the provisions relating to the Government Companies. Chapter XXIV (Sections 396 to 404) deals with Registration Offices and fees (fee structure). Chapter XXV containing Section 405 confers on the Central Government power to direct companies to furnish information or statistics. Chapter XXVI containing Section 406 deals with Nidhis. Chapter XXVII(Sections 407 to 434) makes provisions for constitution, establishment etc. of National Company Law Tribunal and Appellate Tribunal. Chapter XXVIII (Sections 435 to 446) makes provision for establishment of Special Courts and finally Sections 447 to 470 under Chapter XXIX is miscellaneous provisions relating to punishment, penalties.

Further Companies Act of 2013 contains Seven Schedules as stated below:-

SCHEDULE I:

Table A – Memorandum of Association of a company limited by shares.

Table B – Memorandum of Association of a Company Limited by Guarantee and not having a Share Capital.

Table C – Memorandum of Association of Company Limited by Guarantee and having a Share Capital.

Table D – Memorandum of Association of an Unlimited Company and not having Share Capital.

Table E – Memorandum of Association of an Unlimited Company and having Share Capital.

Table F – Articles of Association of a Company Limited by Shares.

Table G – Articles of Association of a Company Limited by Guarantee and having a Share Capital.

Table H – Articles of Association of a Company Limited by Guarantee and not having Share Capital.

Table I – Articles of Association of an Unlimited Company and having a Share Capital.

Table J – Articles of Association of an Unlimited Company and not having Share Capital.

SCHEDULE II:- Useful Lives to compute depreciation.

SCHEDULE III:- General instructions for preparation of balance sheet and statement of profit and loss of a company.

Part I – Balance Sheet.

Part II – Statement of Profit and Loss.

SCHEDULE IV:- Code for Independent Directors.

SCHEDULE V:-

Part I – Conditions to be fulfilled for the appointment of a Managing or whole-time Director or a Manager without the Approval of the Central Government.

Part II – Remuneration.

Part III – Provisions Applicable to Parts I and II of this Schedule.

Part IV – The Central Government may, by notification, exempt any class or classes of companies from any of the requirements contained in this Schedule.

SCHEDULE VI:- Infrastructural projects/infrastructural facilities.

SCHEDULE VII:- Activities which may be included by companies in their Corporate Social Responsibility Policies.

2. Historical Background

The law relating to companies was governed by the Companies Act, 1956. It was a *mammoth* legislation comprising of 658 Sections divided into 13 Parts and 15 Schedules. As time passed drastic changes took place in company law administration. To meet the changing needs and requirements from time to time, the Companies Act, 1956 was amended several times (25 times) to bring about various changes in the Act. In due course, it was felt necessary to pass a new Act repealing the Old Act of 1956 to provide for new provisions to meet the changed national and international economic environment and further to accelerate the expansion and growth of our economy. For this purpose, a bill entitled "the Companies Bill, 2009" was introduced on 3rd August 2009 in the Lok Sabha along with the Statement of Objects and Reasons appended to the said Bill outlining its salient features. Later, the Bill was referred to the Parliamentary Standing Committee on Finance for necessary examination and to submit its report. The Committee, after examining various aspects of the Bill and suggestions for further amendments to the Old Act, 1956, received by the Central Government, submitted its report with necessary recommendations on 31st August, 2010. The Central Government has taken note of several amendments to the Old Act of 1956 from the stakeholders and numerous recommendations as a consequence thereto, decided to withdraw the Companies Bill, 2009 and decided to introduce a fresh Bill incorporating therein the recommendations of the Parliamentary Standing Committee and suggestions from the Stakeholders. The revised Bill namely, the Companies Bill, 2011 containing so many amendments to the Companies Bill, 2009. The Companies Bill, 2011 has been passed by both the Loksabha on 18-12-2012 and Rajyasabha on 08-08-2013 and revised the assent of the President of India on 29th August, 2013 and published in the Gazette of India (Ext.No.27, Part II, Section 1, dated 30-08-2013). It came on the Statute Book as "The Companies Act, 2013 (18 of 2013)".

The New Act is called "The Companies Act, 2013. Section1 of the Act contains the short title, extent, commencement and

application and shall come into force at once and the remaining provisions of the Act shall come into force on such date/dates as and when the Central Government by notification in the Official Gazette, appoint. The provisions of the Companies Act, 2013 shall apply to –

a) Companies incorporated under this Act or under any previous company law;

b) Insurance companies, except in so far as the said provisions are inconsistent with the provisions of the Insurance Act, 1938 or the Insurance Regulatory and Development Authority Act, 1999;

c) Banking companies, except in so far as the said provisions are inconsistent with the provisions of the Banking Regulation Act, 1949;

d) Companies engaged in the generation or supply of electricity, except in so far as the said provisions are inconsistent with the provisions of the Electricity Act, 2003;

e) Any other company governed by any special Act for the time being in force, except in so far as the said provisions are inconsistent with the provisions of such special Act; and

f) Such body corporate, incorporated by any Act for the time being in force, as the Central Government may, by notification, specify in this behalf, subject to such exceptions, modifications or adaptation, as may be specified in the notification and according to sub-section (3) of Section1; the Central Government have issued the notification of enforcement of specified sections of the said Act is as follows:

Notification No.SO 2754(E), Dt.12-09-2013

In exercise of the powers conferred by sub-section (3) of Section 1 of the Companies Act, 2013 (18 of 2013), the Central Government hereby appoints the 12th day of September, 2013 as the date on which the following provisions of the said Act shall come into force, namely –

Section 2 Clause (1); Clauses (3) to (6) (both inclusive); Clauses (8) to (12) (both inclusive); Clauses (14) to (22) (both inclusive); Clauses (24) to (28) (both inclusive); Clauses (29) [except sub-clause (iv); Clause (30); Clauses (32) to (40) (both inclusive); Clauses (43) to (46) (both inclusive); Clauses (49) to (61) (both inclusive); Clauses (63) to (66) (both inclusive); Clause (67) [Except sub-clause (ix)]; Clause (84); Clause (86); Clause (87) [except the proviso and Explanation (d)]; Clauses (88) and (89); Clauses (90) to (95) (both inclusive).

1. Section 19.
2. Section 21.
3. Section 22.
4. Section 23 [except clause (b) of sub-section (1) and sub-section (2)].
5. Section 24.
6. Section 25 [except sub-section (3)].
7. Sections 29 to 32 (both inclusive).
8. Section 33 [except sub-section (3)].
9. Section 34.
10. Section 35 [except clause (e) of sub-section (1)].
11. Sections 36 to 38 (both inclusive);
12. Section 39 [except sub-section (4)];
13. Section 40 [except sub-section (6)];
14. Section 44 and 45;
15. Sections 49 to 51 (both inclusive);
16. Sections 57 to 60 (both inclusive);
17. Section 65;
18. Section 69;
19. Section 70 [except sub-section (2)];
20. Section 86;
21. Section 91;
22. Section 100 [except sub-section (6)];
23. Section 102;
24. Section 103;
25. Section 104;
26. Section 105 [except the third and fourth proviso of sub-section (1) and sub-section (7)];
27. Section 106;
28. Section 107;
29. Section 111;
30. Section 112;
31. Section 113; [except clause (b) of sub-section (1)];
32. Section 114;

33. Section 116;
34. Section 127;
35. Section 133;
36. Section 161 [except sub-section (2)];
37. Section 162 and 163;
38. Section 176;
39. Sections 180 to 183 (both inclusive);
40. Section 185;
41. Section 192;
42. Section 194;
43. Section 195;
44. Section 202;
45. Section 379;
46. Sections 382 and 383;
47. Section 386 [except clause (a)];
48. Section 394;
49. Section 405;
50. Sections 407 to 414 (both inclusive);
51. Section 439;
52. Sections 443 to 453 (both inclusive);
53. Sections 456 to 463 (both inclusive);
54. Sections 467 to 470 (both inclusive);

Notification No.SO 582 (E), Dt.27-02-2014

In exercise of the powers conferred by sub-section (3) of Section 1 of the Companies Act, 2013 (18 of 2013), the Central Government hereby appoints the 1st day of April, 2014 as the date on which the provisions of Section 135 and Schedule VII of the said Act shall come into force.

Notification No.SO 902 (E), Dt.26-03-2014

In exercise of the powers conferred by sub-section (3) of Section 1 of the Companies Act, 2013 (18 of 2013), the Central Government hereby appoints the 1st day of April, 2014 as the date on which the following provisions of the said Act shall come into force, namely–

1. Section 2
2. Clause (2);
3. Clause (7);
4. Clause (13);
5. Clause (31);
6. Clause (41);
7. Clause (42);
8. Clause (47) and clause (48);
9. Clause (62);
10. Clause (83);
11. Clause (85);
12. Explanation (d) of clause (87);
13. Section 3 to 6 (both inclusive);

14. Section 7 [except sub-section (7);
15. Section 8 [except sub-section (9)];
16. Section 9 to 13 (both inclusive);
17. Section 14 [except second proviso to sub-sections (1) and (2)];
18. Sections 15 to 18 (both inclusive);
19. Section 20;
20. Clause (b) of sub-section (1) and sub-section (2) of section 23;
21. Sub-section (3) of section 25;
22. Sections 26 to 28 (both inclusive);
23. Sub-section (3) of section 33;
24. Clause (e) of sub-section (1) of section 35;
25. Sub-section (4) of section 39;
26. Sub-section (6) of section 40;
27. Section 41 and 42 (both inclusive);
28. Section 43;
29. Sections 46 and 47 (both inclusive);
30. Sections 52 to 54 (both inclusive);
31. Section 55 except sub-section (3);
32. Section 56;
33. Section 61 [except proviso to clause (b) of sub-section (1)];
34. Section 62 [except sub-sections (4) to (6)];
35. Sections 63 and 64 (both inclusive);
36. Sections 67 and 68 (both inclusive)
37. Sub-section (2) of section 70;
38. Section 71 (except sub-sections (9) to (11)];
39. Section 72;
40. Section 73;
41. Sub-section (1) of section 74;
42. Section 76;
43. Sections 77 to 85 (both inclusive);
44. Sections 87 to 90 (both inclusive);
45. Sections 92 to 96 (both inclusive);
46. Sub-section (6) of Section 100;
47. Section 101;
48. Third and Fourth proviso to sub-section (1) and sub-section (7) of section 105;
49. Sections 108 to 110 (both inclusive);
50. Clause (b) of sub-section (1) of section 113;
51. Section 115;
52. Sections 117 and 118 (both inclusive);
53. Section 119 [except sub-section (4)];
54. Sections 120 to 122 (both inclusive);

55. Section 123;
56. Section 126;
57. Sections 128 and 129 (both inclusive);
58. Section 134;
59. Sections 136 to 139 (both inclusive);
60. Section 140 [except second proviso to sub-section (4) and sub-section (5)];
61. Sections 141 to 160 (both inclusive);
62. Sub-section (2) of Section 161;
63. Sections 164 to 168 (both inclusive);
64. Section 169 except sub-section (4);
65. Sections 170 to 172 (both inclusive);
66. Sections 173 to 175 (both inclusive);
67. Sections 177 to 179 (both inclusive);
68. Section 184;
69. Sections 186 to 191 (both inclusive);
70. Section 193;
71. Sections 196 to 201 (both inclusive);
72. Sections 203 to 205 (both inclusive);
73. Sections 206 to 209 (both inclusive);
74. Section 210;
75. Section 211;
76. Section 212l, [except references of sub-section (10) of section 66, sub-section (5) of section 140, section 213, sub-section (1) of section 251 and sub-section (3) of section 339 made in sub-section (6) and also sub-sections (8) to (10)];
77. Sections 214 and 215;
78. Section 216 [except sub-section (2)];
79. Section 217;
80. Sections 219 and 220 (both inclusive);
81. Section 223;
82. Sections 224 and 220 (both inclusive)[except sub-section (2) and (5);
83. Section 225;
84. Sections 228 and 229 (both inclusive);
85. Sections 336 to 369 (both inclusive);
86. Section 370 (except the proviso);
87. Section 371;
88. Section 374;
89. Sections 380 and 381 (both inclusive);
90. Sections 384 and 385 (both inclusive);
91. Clause (a) of section 386;
92. Sections 387 to 390 (both inclusive);

93. Sub-section (1) of section 391;
94. Sections 392 and 393 (both inclusive);
95. Section 395;
96. Sections 396 to 398 (both inclusive);
97. Section 399 [except reference of word 'Tribunal' in sub-section (2)];
98. Sections 400 to 404 (both inclusive);
99. Section 406;
100. Section 442;
101. Sections 454 and 455(both inclusive);
102. Section 464;
103. Schedule – I;
104. Schedule – II;
105. Schedule – III;
106. Schedule – IV;
107. Schedule –V;
108. Schedule – VI.

S.O. 1934(E), dt. 1-6-2016: In exercise of the powers conferred by sub-section (3) of section 1 of the Companies Act, 2013 (18 of 2013), the Central Government hereby appoints the 01st day of June, 2016 as the date on which the following provisions of the said Act shall come into force, namely:–

Sl. No.	Section
1.	Sub-section (7) of section 7 [except clause (c) and (d)]
2.	Second proviso to sub-section (1) of section 14
3.	Sub-section (2) of section 14
4.	Sub-section (3) of section 55
5.	Proviso to Clause (b) of sub-section (1) of section 61
6.	Sub-sections (4) to (6) of section 62
7.	Sub-sections (9) to (11) of section 71
8.	Section 75
9.	Section 97
10.	Section 98
11.	Section 99
12.	Sub-section (4) of section 119
13.	Section 130
14.	Section 131
15.	Second proviso to sub-section (4) and sub-section (5) of sec. 140
16.	Sub-section (4) of section 169

17.	Section 213
18.	Sub-section (2) of Section 216
19.	Section 218
20.	Section 221
21.	Section 222
22.	Sub-sections (5) of section 224
23.	Sections 241, 242 [except clause (b) of sub-section (1), clause (c) & (g) of sub-section (2)], 243, 244, and 245
24.	Reference of word 'Tribunal' in sub-section (2) of section 399
25.	Sections 415 to 433 (both inclusive)
26.	Sub-section (1)(a) and (b) of section 434
27.	Sub-section (2) of section 434
28.	Section 441
29.	Section 466

Noti. No. S.O. 630(E), dt. 9-2-2018: In exercise of the powers conferred by sub-section (2) of section 1 of the Companies (Amendment) Act, 2017 (1 of 2018), the Central Government hereby appoints the 9th February, 2018 as the date on which the following provisions of the said Act shall come into force, namely:–

Sl. No.	Section
1.	Section 2 [except clause (i) and clause (xiii)] and section 3;
2.	Section 7;
3.	Section 9;
4.	Sections 11 and 12;
5.	Section 14;
6.	Section 17;
7.	Sections 27 to 29 (both inclusive);
8.	Section 32;
9.	Sections 34 and 35;
10.	Section 38;
11.	Sections 41 to 45 (both inclusive);
12.	Sections 47 and 48;
13.	Sections 50 and 51;
14.	Section 53;
15.	Sections 59 and 60;

16. Sections 63 to 65 (both inclusive);
17. Sections 72 to 74 (both inclusive);
18. Section 77 to 79 (both inclusive);
19. Section 82;
20. Sections 84 and 85;
21. Sections 90 to 93(both inclusive).

3. Changes brought about by the Act

The Companies Act, 2013 brought about significant changes over the Old Act (i.e. the Companies Act, 1956). Notable among them are stated below –

1. The Companies Act, 2013 (18 of 2013) contains 470 sections divided into 29 Chapters and 7 Schedules replaced/repealed Old Act i.e. The Companies Act, 1956, which consisted of 658 Sections divided into 13 Parts and 15 Schedules.
2. Many new Chapters namely Chapter XVII: Registered Valuers, Chapter XXIII: Government Companies, Chapter XXVI: Nidhis; Chapter XXVII: National Company Law Tribunal and Appellate Tribunal; Chapter XXVIII: Special Courts etc. have been incorporated under the New Act.
3. The New Act has made provision for the establishment of **"One Person Company"** under Section 2 (62) of the Act, 2013. Thus, for formation of a Private Limited Company, the minimum number of members has been reduced from two to one. Therefore, a single individual alone can start a company known as "One Person Company".
4. Section 7 of the New Act confer on **Tribunal, Power to Cancel Registration** of a company by deleting its name from the Register of Companies, if a company is found guilty of furnishing false information by suppressing the material facts for getting the company registered.
5. Previously i.e. under the Old Act, there were ten types of Companies: The New Act, has increased the types of Companies from 10 to 15.

6. The New Act envisages **Speedy Incorporation Process** with detailed declarations and disclosures about the promoters, directors etc. at the time of incorporation (Section 7).
7. Section 4(4) and 4(5)(i) of the Act of 2013 incorporate the procedural aspects of applications for availability of the name of proposed company or proposed new name for the existing company. (There is no such provision in the Old Act of 1956).
8. Articles of Association contain entrenchment provisions (no such provisions in the Old Act of 1956).
9. The Directors, Promoters, Experts etc. are personally liable without any limitation for misstatement of prospectus issued with an intent to defraud the applicants for subscription of share capital.
10. Every listed company is required to file a return with the Registrar of Companies furnishing the change of any 2% or more in shareholding position of the promoters and also the top ten share-holders of the Company.
11. Every Company should have at-least one director resident in India, who has stayed for a period of not less than 182 days in the previous calendar year (Section 149).
12. Independent directors to be appointed on the Boards of such companies as may be prescribed. The requirement to appoint minimum number of independent directors, where applicable, to listed public companies is one-third of the total number of directors. For other public companies, the requirement and number may be prescribed through rules. In addition to the concept of Independent Directors (IDs) introduced, the provisions in respect of their tenure and liability, etc., have been provided. Code of IDs provided in a new Schedule to the Act. Databank for ID proposed to be maintained by a body/institute notified by the Central Government to facilitate appointment of IDs. (Section 149).
13. The maximum number of Directors for a public limited company has been increased from 12 to 15. The maximum number of members can be raised beyond 15 by share-holders with a 75% majority by voting. For this purpose the approval/ ratification by the Government of India is not necessary as prescribed under the old Act, 1956.

Further one person can hold directorship (a single individual can be a director) in 20 different companies (as against 15 companies under the old Act, 1956). Out of the 20 companies, he/she cannot be a director for more than 10 public limited companies.

14. According to the New Act, a company must have a registered office on and from the 15th day of its incorporation. (According to the Old Act of 1956, the company should have a registered office from 30th day of incorporation or from the date of the commencement of business).
15. The period of notice to the Registrar of Companies with regard to change of registered office has been reduced to 15 days. (It was 30 days under the Old Act, 1956).
16. For conversion of Public Limited Company into private limited company, approval of the Tribunal is required. [Under the Old Act, it was to be approved by the Central Government (and the Registrar of Companies under the power of delegation)].
17. The New Act prohibited the issue of shares at a discount except sweat equity share. (Section 79 of the Old Act, 1956 permitted the issue of shares at a discount subject to certain conditions).
18. As per the New Act full annual return should be filed every year enclosing details as on the closing of financial year. (but not once in 5 years as per Old Act).
19. The New Act prescribes punishment to company secretary from Rs.50,000/- to Rs.5,00,000/- for fraudulent certification of annual returns. (No such penal provision in the Old Act).
20. On and after the commencement of the Companies Act, 2013, only the following companies may invite accept or renew deposits from the public:
    i) Banking companies;
    ii) Non-banking Financial Company (NBFCs);
    iii) Notified Companies;
    iv) Public Company having such net worth or turnover as may be prescribed as per audited balance sheet of the immediately preceding financial year;
    v) Companies other than those covered in (i) to (iv) above shall not invite, accept or renew deposits from the public

(i.e. persons other than members). Whatever deposits were accepted by companies other than those covered in (i) to (iv) above before the commencement of the Act shall be repaid by them within one year from the commencement of the Companies Act, 2013 or from the date on which payments are due whichever is earlier (Sections 73 to 76).

21. The rehabilitation and Revival Fund as provided in the Companies (Second Amendment) Act, 2002 is to be replaced by Rehabilitation and Insolvency Fund with voluntary contributions linked to entitlements to draw money in a situation of insolvency.

22. Unpaid and unclaimed dividend amount shall be deposited in a scheduled bank by opening a special account called **"Unpaid Dividend Account".** (Section 124).

23. The new Act under Section 129, made it mandatory for Companies having subsidiary companies (i.e. Holding Company and Subsidiary Companies) to prepare **"Consolidated Financial Statements".** The word "subsidiary" under the Act includes associate and joint venture company.

24. A meeting of the Board may be called at shorter notice subject to the condition that at least one independent director, if any, shall be present. However, in the absence of any independent director from such meeting the decision taken shall be final only on ratification by at-least one independent director [Section 173(3)].

25. The Act under Section 406, made provision for creation of Nidhi. Nidhi means "a company which has been incorporated as a Nidhi with the object of cultivating the habit of thrift and savings among its members (Section 406).

26. Section 435 of the Act confers on Central Government, empowered to establish Special Courts in constitution with Chief Justice of the High Court within whose jurisdiction the Judge is to be appointed (Section 435).

27. The Special Court would have the liberty to try summary proceedings for offences punishable with imprisonment for a term not exceeding three years (Section436).

28. The New Act makes provision for merger or amalgamation of a company with a foreign company (Section 234).

29. The Act under Section 455 made provision for registration of a **"Dormant Company"**. Dormant Company means "a company registered for a future project or to hold an asset or intellectual property and has no significant accounting transaction, may make an application to the Registrar for obtaining the status of dormant or inactive company.

4. New Provisions/Concepts introduced under the Act, 2013

1. The significant development of the New Act is, the concept of "One Person Company" (OPC) has been introduced (irrespective of minimum number of two and seven for formation of a Private Limited and Public Limited Companies respectively under the Old Act, 1956).

2. The New Act under Section 4(5) confers on the Registrar of Companies (ROC) power to delete/strike off the name of a company from the registrar of incorporation, if it is found guilty of furnishing false information by suppressing the material facts at the time of registration.

   Similar power under Section 7 has been conferred on the Tribunal to cancel the registration.

3. The New Act introduced voting by electronic means by the members at meetings.

4. National Financial Reporting Authority (NFRA) instead of National Advisory Committee on Accounting Standards (NACAS). NFRA, unlike NACAS, is not merely an advisory body. NFRA is charged with responsibility to monitor and enforce compliance with accounting and auditing standards recommended by it.

   Further NFRA empowered to investigate into professional or other misconduct of CAs and impose penalties of not less than Rs.1,00,000/- and not exceeding 5 times the fees received in case of individuals and not less than Rs.1,00,000/- and not exceeding 10 times the fees received in case of firms and debar member/firm for a period of 6 months to 10 years (Sec. 132).

5. Internal audit by CAs/CWAs/such other professional as may be decided by the Board proposed to be made mandatory for prescribed classes of Companies (Section 138).

Mandatory rotation of auditors for listed companies and other prescribed clauses of companies after 5 years in case of auditor who is individual CA and after 10 years for auditor which is a CA firm (Section 139).

Tribunal may direct a company to change its auditors if it is satisfied that auditors have acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its officers or directors (Section 140).

6. The new Act makes it mandatory, appointment of certain committees of Directors for listed and other classes of companies as stated below –

i) Audit Committee.

ii) Nomination and Remuneration Committee.

iii) Stakeholders' Relationship Committee (Section 178).

Corporate Social Responsibility (CSR) Committee of the Board proposed in addition to other committees of the Board Viz. Audit Committee, Nomination and Remuneration and Stakeholders Relationship Committee. These Committees shall have IDs, non-executive directors to bring more independence in Board functioning and for protection of interests of minority shareholders.

7. The New Act made provision for video conference by electronic means in Board of Directors' meetings (Section 154). Such participation shall be counted for the purpose of ***'quorum'*** (Section 173).

8. The new Act prescribed investigation into the affairs of the company by Serious Fund Investigation Office (SFIO) (Section 211).

9. Class action against oppression/mis-management by member/members or by creditor/creditors (Section 245) shareholders associations or group of shareholders/ depositors to be enabled to take legal action in case of any fraudulent action on the part of a company and to take part in investor protection activities and 'Class Action Suits'.

10. Application by company by special resolution or consent of 75% of members in terms of share capital to Register of Companies (ROC) for removing name of the company from register (Section 248).

11. Revival and Rehabilitation of sick companies (Chapter XIX) (Sections 253-269).

12. The Act under Section 435 made provision for establishment of Special Courts to try offences under the Act.

5. Provisions under the Old Act, 1956 discarded/ deleted by the New Act, 2013

The following provisions of Companies Act, 1956 (Section number in parentheses are of Act, 1956) have not been incorporated in Companies Act, 2013 and omitted them from the new Act of 2013.

1. Certificate of incorporation is the conclusive evidence (Section 35).
2. Statement in lieu of prospectus (Section 70).
3. Share Warrants (Section 114).
4. Provisions relating to certificate of commencement of business (Section 149).
5. Public Trustee (Section 153.A).
6. Statutory meeting and statutory report (Section 165).
7. Payment of interest out of capital (Section 208).
8. Special audit (Section 233-A).
9. Share Qualification (Section 270).
10. Restrictions on appointment and remuneration of sole selling and sole-purchasing agents (Sections 294 to 294.AA).
11. Employees Securities and P.F (Section 417).
12. Receivers and managers (Sections 421 to 424).

Lecture – II

COMPANY: MEANING, DEFINITION AND KINDS

This lecture covers –

1. Company: Meaning and Definition.
2. Features of a Company.
3. Kinds of Companies.
4. Private Company and Public Company.
5. Company and Partnership.
6. Company distinguished from Hindu Undivided Family.
7. Nature of Company
   - i) Is Company a Citizen?
   - ii) Nationality, Domicile and Residence of a Company.
   - iii) Company is a Corporation or Body Corporate?
   - iv) Body Corporate:
     - a) Corporate Sole.
     - b) Corporation and
     - c) Corporate Aggregate.

1. Company: Meaning and Definition

When a business is carried on by a single person, it is called 'Sole Trading Concern'. When a business is carried on by two or more persons, subject to a maximum of ten in case of banking business and twenty in case of a non-banking business, it is called partnership firm. If the business is to be carried on a large scale, the alternative resort is company business. A Company may be a private company or a public company. Earlier, the law relating to companies is governed by the Indian Companies Act, 1956. It has been replaced by the Companies Act, 2013. Now, the law relating to companies is governed by the Companies Act, 2013 (Act 18 of 2013).

Meaning: Strictly speaking, the word company has no technical or legal meaning. It literally means "a group or association of persons, who have agreed to undertake a predetermined venture." Etymologically speaking, the word 'Company' is derived from the Latin word 'com' and 'panies'. 'Com' means with or together; and 'panis' means bread. The words referred to an association of persons, who took their meals together. In *Smith vs. Anderson*, a company in broad sense may mean 'an association of individuals formed for some'.

A Company has no strictly technical or legal meaning. A Company in common parlance means 'an artificial (fictitious) person created by law with perpetual existence and common seal'. The word 'artificial' denotes, it has no body or soul. In simple, a company by itself is not a living person and its living persons viz. directors, employees etc. act on its behalf. It is created by law, in the sense, so many legal formalities are required to be fulfilled for formation/ registration of a company. The expression 'perpetual existence' means, it is not dissolved by death, insanity/insolvency/bankruptcy of any of its members. In other words, men may come and men may go, but company goes on forever till it is wound up (men = directors, employees, shareholders etc.). The words 'common seal' signifies its assent to any document or contract. Company being an artificial (non living) person, it cannot act by itself and hence its directors, officials etc. act on its behalf. The rubber stamp of a company contains for example: 'For Hindustan Shipyard Limited... Managing Director.' 'For Andhra Steels Private Limited... Chief Personnel Manager' etc.

Definition: It is difficult to define company. However, many attempts were made in this context, prominent among them are detailed below.

Lindley's Definition: 'By a company is meant as association of many persons who contribute money or money's worth to a common stock and employ it for a common purpose. The common stock so contributed is denoted in money, and is the capital of the Company. The persons who contribute to it or to whom it belongs

are the members. The proportion to which each member is entitled is his share.'

Justice James: 'A Company is an association of persons united for common object'.

Blackstone: 'The company never dies. It is an entity with perpetual succession. Perpetual succession means that the membership of a company may keep changing from time to time, but that does not affect the company's continuity in the link manner as the river Thames is still the same river, though the parts which compose it are changing every instant.'

Prof.Haney: He defines Company as "an incorporated association which is an artificial person created by law, having separate entity, with a perpetual succession and a common seal."

The most accepted definition of word Company propounded by Lindley reads as follows:

"By a company is meant associations of many persons who contribute money or money's worth to a common stock and employ it for common purpose. The common stock so contributed is denoted in money and is the capital of the company. The persons who contribute it or to whom it belongs are members. The proportion of capital to which each member is entitled is his share".

In view of the above definitions of the term "Company" it is submitted that the company is a juristic person with perpetual succession and common seal and in which shares are transferable, however, with limited liability. The Apex Court in *M/s. Electronics Corporation of India Ltd. V. Secretary, Revenue Department, Government of A.P. and others* (AIR 1999 SC 1734) observed that "A company registered under the Companies Act, 1956 is a distinct legal entity/personality other than the legal entity or entities that holds its shares."

The above definitions are not satisfactory Firstly, it is not necessary for a company to be consisted of many individuals. A private company may be formed by two persons and a public company by seven persons. Secondly, a company has an entity

distinct from its members and, therefore, it is not correct to state that a company possesses the capacity 'of enjoying privileges and immunities in common.'

Section 2(10) of the Companies Act, 1956: Section 2(10) of the Companies Act, 1956 defines firstly that 'Company' means a company as defined in Section 3. Section 3(1)(i) states that 'company' means a company formed and registered under this Act, or an existing company. An 'existing company' means a company formed and registered under any of the former Companies Acts.

Section 2(20)of the Companies Act, 2013: According to Section 2(10) of the new Act, 2013, 'Company' means "a company incorporated under the Companies Act, 2013 or other previous law governing/regulating companies/company business.

Section 3(1)(i): Section 3(1)(i) of the Companies Act, 1956 defines 'Company' – 'Company means a company formed and registered under this Act or an existing company as defined in Clause (ii). Existing company means a company formed and registered under any of the previous companies laws.

Section 3(1) of the Indian Companies Act, 1956 defines company as 'a company formed and registered under this Act or an existing company'. An existing company means 'a company, which was in existence at the time of commencement of the Act'.

2. Features or Characteristics of a Company

Following are the features of a joint stock company.

i. Artificial Person.

ii. Voluntary Association.

iii. Perpetual Existence.

iv. Legal Entity.

v. Transferability of shares.

vi. Limited Liability.

vii. Capacity to sue and be sued.

i. Artificial Person: Company is an artificial person created by law. Artificial in the sense, it has no body or soul like a natural person. Created by law means formation of a company requires fulfillment of so many legal formalities.

ii. Voluntary Association: Company is a voluntary association of persons to carry on some business. There is nothing to prevent them from not coming together.

iii. Perpetual Existence: The outstanding feature of a company is, its independent corporate existence. In other words, it is a distinct legal person existing independent of its members. Its members may come and go, but it goes on forever till it is wound up. In other words, a company is not dissolved by the death or insanity or bankruptcy of any of its members except by the process of liquidation/winding up. The life of a company usually depends upon the terms of its Memorandum of Association. It may come into existence for a limited period of years or may continue perpetually. When it is incorporated for a limited period, its life will be ceased to exist by way of voluntary winding up even though it is in solvent position. The Bombay High Court in – *T.R.Pratt (Bombay) Ltd. V. E.D.Sassoon* (AIR 1936 Bom. 62):

"An incorporated company is a distinct entity and although all the shares may be practically controlled by one person, in law a company is a distinct entity and it is not permissible or relevant to enquire whether the directors belonged to the same family or whether it is, as compendiously described a 'one man company'."

iv. Legal Entity: Every joint stock company, whether private limited or public limited must be registered. On registration/ incorporation, a company is conferred legal personality/corporate personality, by which it gets separated from its members. In simple words, before incorporation the company and its members were one and the same and the company is answerable for the acts of its members (i.e. promoters and the members, who signed the Memorandum). After registration/incorporation, the company gets separated from its members. A veil or corporate veil is created between the company and its members and the company is not

liable/answerable for the acts/wrongs committed by its members (Salman v. Salman & Co. Ltd (1897) A.C. 22). It acquires such rights and powers as a human being. In other words, it gets separate legal entity. In the eyes of law, it is regarded as an independent person and gets separated from its members. Such independent legal personality is called corporate personality (Section 9). It can own properties in its own name. It can sue and be sued in its own name.

v. Transferability of shares: The ownership of a company is vested in several members called shareholders, who contribute invest money/capital by way of purchasing shares of the company. Any shareholder can transfer his shares in a manner provided by the articles of association.

Section 44 of the Companies Act, 2013 provides for transfer of shares. It reads as follows:

"The [shares or debentures] or other interest of any member in a company shall be movable, transferable in the manner provided by the articles of the company."

vi. Limited Liability: The liability of members (shareholders) is limited to the extent of face value of the shares, where the company is limited by shares. Then, the shareholder is liable to the extent of unpaid capital on his shares and his personal assets/properties will not be affected in the event of winding up of the company.

However, in case of a company, limited by guarantee, each member (shareholder) is liable to contribute a specified amount to the assets of the company in the event of its being wound up. In other words, the liability of members of such company is restricted to the nominal value of the shares taken by them or the amount guaranteed by them, whichever is more/higher.

vii. Capacity to sue and be sued: A company has a distinct legal personality. Being a legal person, a company can sue and be sued in its own name. Unlike partnership and action against a company does not mean an action against its members.

3. Kinds of Companies

Companies are classified into different categories as follows:

A) On the basis of Incorporation
   1. Unincorporated Company and
   2. Incorporated Company
      i) Chartered Company
      ii) Statutory Company and
      iii) Registered Company

B) On the basis of Liability
   1. Unlimited Company (Section 2(92) and
   2. Limited Company
      i) Company limited by shares (Section 2(22)) and
      ii) Company limited by guarantee (Section 2(21))

C) On the basis of Control
   1. Holding Company (Section 2(46)) and
   2. Subsidiary Company (Section 2(87))

D) On the basis of Ownership
   1. Government Company (Section 2(45)) and
   2. Non-Government Company

E) Other kinds of Companies
   1. Banking Company (Section 2(9))
   2. Foreign Company (Section 2(42))
   3. One Person Company
   4. Dormant Company (Section 455) and
   5. Defunct Companies (Section 248)

A) On the basis of Incorporation

On the basis of incorporation, companies may be divided into the following categories.

1. Unincorporated Companies

These companies are also known as 'Common Law Companies'. They are constituted by contract. An unincorporated company has no legal personality distinct from its members. The liability of its members is unlimited. Such companies are rarely formed. At present, such companies can no longer be formed under the Companies Act, 1956.

2. Incorporated Companies

An incorporated company is one, which is formed for the purpose of carrying business to earn profit. These companies are incorporated either by the Companies Act, 2013 or some other Companies Acts before 2013 (i.e. before the passing of the Companies Act, 2013 viz. the Companies Act, 1956 and earlier). They are divided under three categories namely:

i) Chartered Companies.

ii) Statutory Companies; and

iii) Registered Companies.

i) Chartered Companies: A chartered company is one, which is created/established under the Royal Charter issued by the Crown (The hereditary monark, the King or Queen in England). The best example for the chartered company is the East India Company, which was established in 1600 A.D. under the charter of 1600 issued by the then Queen Eligibeth-I on 31-12-1600. A chartered company enjoys an unrestricted corporate capacity. It can do any such act even if the charter expressly forbids to do such act. At present, there are no such companies in India.

ii) Statutory Companies: A statutory company is one, which is incorporated by a special Act of the legislature. They relate to public utility services namely railways, roadways, electricity etc. The best examples of the statutory companies are, The Reserve Bank of India, The State Bank of India, The Life Insurance Corporation of India etc. The object, powers, privileges, obligations etc. of these statutory companies are defined by the respective Act under which

they were established. For instance, the Reserve Bank of India was established under the Reserve Bank of India Act, 1935. They are not required to have any Memorandum of Association or Articles of Association. A statutory company enjoys legal/corporate personality distinct from its members.

iii) Registered Companies: A registered company is one, which is registered/ incorporated with the Registrar of the Joint Stock Companies under the Companies Act, 2013 or earlier viz. the Companies Act 1956 or any of the or were registered earlier Companies Acts. Most of the Companies in India are registered companies i.e. registered/ incorporated with the Registrar of the Joint Companies under the Companies Act, 2013 or earlier Companies Act.

B) On the basis of Liability

On the basis of liability, the registered companies are categorized as follows —

1. Unlimited Company (Section 2(93).
2. Limited Company
   a) Company Limited by Shares (Sec.2(22) and
   b) Company Limited by Guarantee (Sec.2(21)

1. Unlimited Company (Section 2(92): According to Section 2(92) of the Companies Act, 2013 'unlimited company' means a company not having any limit on the liability of its members.

Section 3(2)(c) of the Companies Act 2013 permits unlimited liability by the members (shareholders). The liability of members extends to their private property as in the case of sole trader or partnership firm. If assets of the company are insufficient to pay off the liabilities in full, members will be required to pay an unlimited amount to meet the deficiency. However, the creditors cannot proceed (sue) against the personal assets of the shareholders. Such unlimited companies are rarely to be found these days.

2. Limited Company: Limited Company is a joint-stock Company the liability of the members of which for the debts of the company is limited by statute. They are of two types:

i) Company limited by shares (Section 2(22)): A company limited by shares has a share capital, and the liability of each member is limited to the value of the share held by him. If he has already paid part of the value, his liability remains to the extent of the unpaid amount. If shares are fully paid, the liability of the member in respect of such shares is no more there. Even if a company runs into huge losses a shareholder cannot be called upon to pay more than the value of the shares agreed to be taken by him. In simple words, the members/shareholders are liable for face value of the shares only since their liability is limited.Most of the companies operating today belong to this type. A company limited by shares may be Public Company or a Private Company.

ii) Company limited by Guarantee (Sec.2(21):The members may undertake liability beyond the face value to meet the liability at the time of winding up of the company. It is contained in the Memorandum of Association of the Company.

C) On the basis of Control

On Companies, on the basis of control can be classified into two heads namely –

1. Holding Company (Section 2(46) and
2. Subsidiary Company (Section 2(87).

Where the relationship between two companies is such that, one company controls the other, the controlling company is called 'Holding Company', while the controlled company is called 'Subsidiary Company'.

1. Holding Company (Section 2(46): According to Section 2(46) of the Companies Act, 2013, 'holding company', in relation to one or more other companies, means a company of which such companies are subsidiary companies.

Holding company is a Corporation organized to hold the stock of another or other Corporation. When a company has control over another company, it is known as a 'holding company'. Under any of the three following circumstances, a company should be called a holding company of the other company, if

i) It controls the composition of the Board of Directors.

ii) It is controlling the affairs of a company which is also controlling the affairs of some other companies.

iii) Its preference shareholders have the same voting rights as given to equity shareholders and they control more than half the total voting power of another company.

2. Subsidiary Company (Section 2(87): According to Section 2(87) of the Companies Act, 2013 *"subsidiary company"* or "subsidiary", in relation to any other company (that is to say the holding company), means a company in which the holding company:

(i) controls the composition of the Board of Directors; or

(ii) exercises or controls more than one-half of the total voting power either at its own or together with one or more of its subsidiary companies:

Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.

Explanation: For the purposes of this clause:

(a) a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clause (*i*) or sub-clause (*ii*) is of another subsidiary company of the holding company;

(b) the composition of a company's Board of Directors shall be deemed to be controlled by another company if that other company by exercise of some power exercisable by it at its discretion can appoint or remove all or a majority of the directors;

(c) the expression "company" includes any body corporate;

(d) "layer" in relation to a holding company means its subsidiary or subsidiaries;

Illustration of subsidiary company: Company 'B' is a subsidiary of Company 'A', and Company 'C' is a subsidiary of

Company 'B'. Company 'C' is a subsidiary of Company 'A' too. If Company 'D' is a subsidiary of Company 'C', Company 'D' will be a subsidiary of Company 'B' and consequently also of Company 'A'.

D) On the basis of Ownership

On the basis of ownership, companies may be divided into two heads namely –

1. Government Company (Section 2(45)) and
2. Non-Government Company.

1. Government Company (Section 2(45)): According to Section 2(45) of the Companies Act, 2013, *"Government company"* means any company in which not less than fifty-one per cent. of the paid-up share capital is held by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, and includes a company which is a subsidiary company of such a Government company;

Heavy Engineering Corporation Limited (HECL), Hindustan Machine Tools Limited (HMT), State Trading Corporation of India Limited (STCIL) are examples of Government Companies.

2. Non-Government Company: Non-Government Company means a company which is not a Government Company. A non-Government company is controlled and operated by private capital. All the provisions of the Companies Act, 1956 are applicable to a non-Government Company.

E) Other Kinds of Companies

In addition to the above, the other kinds of companies are –

1. Banking Company (Section 2(9)).
2. Foreign Company (Section 2(42)).
3. One Person Company (Section 2(62)).
4. Dormant Company (Section 455) and
5. Defunct Companies (Section 248).

1. Banking Company (Sec.2(9): According to Section 2(9) of the Companies Act, 2013 'banking company' means a banking company as defined in clause (c) of Section 5 of the Banking Regulation Act, 1949 (10 of 1949).

A banking company in India has been defined in Section 5(c) of the Banking Regulation Act, 1949 as one 'which transacts the business of banking which means the accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise.'

2. Foreign Company (Sec.2(42)): According to Section 2(42) of the Companies Act, 2013, Foreign Company means any company or body corporate incorporated outside India which –

a) Has a place of business in India whether by itself or through an agent, physically or through electronic mode; and

b) Conducts any business activity in India in any other manner.

Section 379 to 393 of the Companies Act, 2013 deals with Companies incorporated outside India.

3. One person Company (Sec.2(62): According to Section 2(62) of the Companies Act, 2013, 'one person company' means a company which has only one person as a members'. The companies Act, 2013 allows 'one person company' to get registered as private company.

Conditions applicable for incorporation of One Person Company

(1) Only a natural person who is an Indian citizen and resident in India -

(a) shall be eligible to incorporate a One Person Company;

(b) shall be a nominee for the sole member of a One Person Company.

Explanation–For the purposes of this rule, the term "resident in India" means a person who has stayed in India for a period of not

less than one hundred and eighty two days during the immediately preceding one calendar year.

(2) No person shall be eligible to incorporate more than a One Person Company or become nominee in more than one such company.

(3) Where a natural person, being member in One Person Company in accordance with this rule becomes a member in another such Company by virtue of his being a nominee in that One Person Company, such person shall meet the eligibility criteria specified in sub rule (2) within a period of one hundred and eighty days.

(4) No minor shall become member or nominee of the One Person Company or can hold share with beneficial interest.

(5) Such Company cannot be incorporated or converted into a company under section 8 of the Act.

(6) Such Company cannot carry out Non-Banking Financial Investment activities including investment in securities of any body corporates.

(7) No such company can convert voluntarily into any kind of company unless two years have expired from

the date of incorporation of One Person Company, except threshold limit (paid up share capital) is increased beyond fifty lakh rupees or its average annual turnover during the relevant period exceeds two crore rupees.

4. Dormant Company (Sec.455): Where a company is formed and registered under this Act for a future project or to hold an asset or intellectual property and has no significant accounting transaction, such a company or an inactive company may make an application to the Registrar in such manner as may be prescribed for obtaining the status of a dormant company.

5. Defunct Companies (Section 248): The Companies which are not carrying on any business or when they are not in operation are called "defunct companies". By virtue of Section 248(1) of the Companies Act, 2013 the Registrar of Companies is

empowered to remove name of company from register of companies. If he/she has reasonable cause to believe that –

i) Failure to commence business: Company has failed to commence its business within one year of its incorporation.

ii) Non-payment of subscription amount: Omitted by Act 21 of 2015, w.e.f. 29-5-2015.

iii) Non-obtaining of status of dormant company: A company is not carrying on any business or operation for a period of two immediately preceding financial years and has not made any application within such period for obtaining the status of a dormant company under Section 455 (i.e. Dormant Company).

In aforesaid circumstances, the Registrar of Companies shall send a notice to the company and all the directors of the company, of his/her intention to remove the name of the company from the register of companies and requesting them to send their representations along with copies of the relevant documents, if any, within a period of thirty days from the date of notice.

As stated above, there are various kinds of companies. However, the main categories are two, namely –

4. Private Company and Public Company

1. Private Company (Section 2(68)) and
2. Public Company (Section 2(71)).

1. Private Company (Sec.2(68)): According to Section 2(68) of Companies Act, 2013 – *"private company"* means a company having a minimum paid-up share capital [xxx] as may be prescribed, and which by its articles:

(i) restricts the right to transfer its shares;

(ii) except in case of One Person Company, limits the number of its members to two hundred:

Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this clause, be treated as a single member:

Provided further that:

(A) persons who are in the employment of the company; and

(B) persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased,

shall not be included in the number of members; and

(iii) prohibits any invitation to the public to subscribe for any securities of the company;

2. Public Company (Sec.2(71)): According to Section 2(71) of the Companies Act, 2013 –

"public company" means a company which:

(a) is not a private company; and

(b) has a minimum paid-up share capital [xxx] as may be prescribed:

Provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles.

Distinction between Private Company and Public Company

Private Company	Public Company
1. The minimum number of members (except in case of a One Person Company) is two.	1. The minimum number of members is seven.
2. The maximum number of members except in case of One Person Company is two hundred (Fifty under the Act of 1956).	2. The maximum number of members is unlimited (i.e. there is no maximum limit).
3. Shareholders have no right to appeal against the decision of the Board of Directors, if it (Board of Directors) refuses to register the transfer of shares.	3. The shareholders of a Public Company have a right to appeal against the decision of the Board of Directors for refusing to

	register the transfer of their shares.
4. It must have at least two Directors.	4. It must have at least three Directors.
5. Quorum required for meeting is two persons.	5. The quorum for meeting is minimum five persons depending upon number of shareholders as provided under section 103 of Companies Act, 2013
6. Its Profit and Loss Account and Balance Sheet are not open for inspection by the non-members.	6. They are open for inspection by any member of the public.
7. A private company can pay remuneration to it's managerial personnel without any restrictions.	7. A public company shall pay remuneration to it's managerial personnel as per the limits prescribed under Companies Act, 2013.
8. A private company enjoys some special privileges.	8. A public company enjoys no such special privileges.

5. Company and Partnership

Partnership Meaning: 'When two or more persons (Subject a maximumof 50 members) carry on business to share profits and losses equally or in proportion of capitals, it is called partnership business.' The persons are called 'Partners' and the business is called 'Partnership Firm'.

Definition: Section 4 of the Indian Partnership Act, 1932 defines 'Partnership'. 'Partner' 'Firm and Firm Name'.

'Partnership is the relation between persons who have agreed to share the profits of business carried on by all or any of them acting for all.'

'Persons, who have entered into partnership with one another are called individually 'Partners' and collectively 'a firm' and the

name under which their business is carried on is called 'the firm name'.

Essential Features: To constitute partnership, the following ingredients are to be satisfied:

1. Association of two or more persons.
2. Agreement (Partnership Deed).
3. To carry on business.
4. Sharing of profits (equally or in proportion of capital).
5. Mutual agency (one acting for all and all action for one).

1. Association of two or more persons: To constitute partnership, there must be atleast two persons. The maximum number of persons is 50. For partnership gets dissolved if the number comes down to one (i.e. the number of partners is reduced to one).

2. Agreement (Partnership Deed): Partnership is the result of an agreement. Section 5 says that, the relation of partnership arises from contract and not from status. The contract must fulfill the essentials of a valid contract viz. free consent, lawful consideration legality of object etc. under Section 10 of the Indian Contract Act, 1872.

3. To carry on Business: The very purpose of partnership is to carry on business to earn profit. According to Section 2(b) of the Partnership Act, the expression 'business' includes "every trade, occupation and profession". The business may be permanent or temporary or for a specific adventure.

4. Sharing of Profits: The term 'Partnership' is derived from the word 'to part', which means, "to divide". Thus dividing or sharing of profits is an essential feature of partnership and is contained in the partnership agreement/deed. The partners may share profits or losses equally or in proportion of their capitals as stated in the partnership deed. The ratio of sharing profits or losses varies from partnership to partnership.

5. Mutual Agency: The expression 'mutual agency' denotes "business carried on by all or any of them acting for all". In simple

words, "all act for one and every one acts for all". Thus, an act of partner is binding on the firm just like an act of an agent is binding on the principal. Therefore, it is said that "The law of partnership is an extension of the law of agency or law as to partnership is undoubtedly a breach of the law of principal and agent". (The Rule in COX vs. Hickman).

Distinction between Company and Partnership: Following are the notable points of difference between Company and Partnership.

Company	Partnership
1. It is governed by the Indian Companies Act, 2013.	1. It is governed by the India Partnership Act, 1932.
2. Minimum number of members is 7 in case of public company and 2 in case of private Company except in case of One person Company.	2. Minimum number of members (partners) is two.
3. Maximum number of members is 200 in private company and no maximum limit in case of public company.	3. Maximum number of members fifty.
4. Liability is limited.	4 Unlimited Liability.
5. Shares are Transferable without the consent of other members.	5. Shares are not transferable without the consent of other partners.
6. Registration of a Company is compulsory.	6. Registration of a Partnership is optional.
7. A shareholder can contract with the company.	7. A partner cannot contract with the firm.
8. Company is a legal person.	8. Partnership is not a legal person.

Lecture – III

FORMATION OF COMPANY (REGISTRATION AND INCORPORATION)

Earlier, i.e. prior to the passing of the New Companies Act, 2013, Part-II of the Companies Act, 1956 containing Sections 11 to 54 lay down the provisions relating to 'Incorporation of Company and matters incidental thereto'. Now, Chapter II containing Sections 3 to 22 of the Companies Act, 2013 provides for "Incorporation of Company and matters incidental thereto." Section 7 lays down the procedure, information to be furnished and documents to be submitted to the Registrar of Companies for registration of a company, private or public limited company. Section 7, except sub-section (7) came into force on 01-04-2014.

This lecture covers:

1. Incorporation of a company (Section 7).
2. Effects of Incorporation (Section 9).
3. Corporate personality or The Rule in *Solomon vs. Solomon and Company Ltd. and Lifting or Piercing the Corporate Veil.*
4. Promoter and Pre-incorporation Contracts and
5. A company is not a citizen.
6. Distinction between Private Limited Company and Public Limited Company.

1. Incorporation of a Company

A company, whether private limited or public limited must be registered with the Registrar of Companies. On registration, a Certificate of Incorporation is issued by the Registrar. Then, the company is said to have been incorporated and comes into existence.

Seven or more persons in case of public company or two or more persons subject to a maximum of 200 in case of private company (except in case of a 'One Person Company') may associate

for formation of a company to carry on lawful business. Generally, a person called 'Promoter' undertakes formation of a company. He takes necessary steps for incorporation/registration of the company. As provided for under Section 7 of the Companies Act, 2013, the most important documents to be submitted to the Registrar of Companies along with the filled in application and requisite fee are, the Memorandum of Association and Articles of Association.

Procedure for Registration/Incorporation (Section 7): For registration of a Company, an application is in the prescribed Form INC-22/INC-29 shall be filed along with required fee as prescribed with the Registrar of Companies of the State in which the Registered Office of the company is to be situated along with the following documents (Sec.7).

1. Memorandum of Association: It is a very important document to be submitted to the Registrar of Companies as prescribed under Schedule-I of the Companies Act, 2013. According to Section 2(56) of Companies Act, 2013, 'memorandum' means the memorandum of association of a company as originally framed or as altered from time to time in pursuance of any previous company law or of this Act. It contains the relationship of the company with outsiders. The name of the company, its object, situation etc. is contained in the Memorandum. Memorandum, duly signed by the subscribers has to be submitted.

2. Articles of the Association: The second most important document to be submitted to the Registrar of companies for incorporation is the Articles of Association. It is also known as 'Articles of Incorporation.'

According to Section 2(5) of the Companies Act, 2013, 'articles' means the articles of association of a company as originally framed or as altered from time to time or applied in pursuance of any previous company law or of this Act. It contains the constitution, rules, capital structure etc. of the company. The Articles of Association, if any, shall be signed by the subscribers to the Memorandum of Association. A public company limited by shares

need not have its own Articles of Association. As per section 5 of the Companies Act, 2013, every company may adopt model articles as may be applicable to such company.

The Memorandum of Articles are to be signed at least by seven subscribers in case of a public company and two subscribes in case of a private company in the presence of at least one witness. The subscribers should furnish their names, addresses and number of shares subscribed by each of them (in the manner prescribed under Section 7(1)(a).

3. Declaration: A declaration that all the requirements under the Companies Act have been complied with. The declaration has to be signed by any one of the following persons –

a) an Advocate; or

b) a chartered accountant, cost accountant or company secretary in practice,who is engaged in the formation of the company; or

c) a person named in the Articles as a Director, Manager or Secretary of the Company.

4. Affidavit: An affidavit from each of the subscribers to the memorandum and from persons named as the first directors, if any, in the article, that he is not convicted of any offence in connection with the promotion, formation or management of any company; or has not been found guilty of any fraud or misfeasance or any breach of duty to any company under this Act or any previous company law during the preceding five years and that all information filed in the documents filed with the Registrar for registration of the company is correct and complete and true to the best of his knowledge and belief.

Certificate of Incorporation: If the Registrar is satisfied that all the statutory requirements stated aboveare complied with under the Act, will enter the name of the Company in the Register of Companies maintained by him and then issues a certificate called 'Certificate of Incorporation' under his signature as per Section 9 of

the Companies Act, 2013.

Procedure for Incorporation of a Private Company: The procedure for the incorporation of a private company is virtually the same as that of a public company as described as above except with the following exceptions:

i) Only two subscribers to the memorandum are necessary instead of seven.

ii) The company should carefully abide by the provisions of Section 12 of the Companies Act, 2013 while preparing the memorandum and the articles of association.

Effect of Certificate of Incorporation: The certificate of incorporation is a conclusive evidence of the fact that all the requirements of the Companies Act have been complied with and that everything is in order as regards registration and that company is a validly incorporated company. Once the certificate of incorporation is issued by the Registrar the validity of the certificate cannot be challenged on any ground.

From the date of incorporation mentioned in the certificate of incorporation, such subscribers to the memorandum and all other persons, as may, from time to time, become members of the company, shall be a body corporate by the name contained in the memorandum, capable of exercising all the functions of an incorporated company under this Act and having perpetual succession with power to acquire, hold and dispose of property, both movable and immovable, tangible and intangible, to contract and to sue and be sued, by the said name.

Relevant case law:

***Jubilee Cotton mills Ltd. v. Lewis,* (1924) AC 958** – On 6th January, the necessary documents were delivered to the Registrar for registration. Two days after, the Registrar issued the certificate of incorporation but dated it 6th January instead of 8th, i.e. the day on which the certificate was issued. On 6th January some shares were allotted to L, i.e. before the certificate of incorporation was

issued. The question arose whether the allotment was void. Held, the certificate of incorporation is conclusive evidence of all that it contains. In law the company was formed on 6th January and, therefore, the allotment of shares was valid.

***MoosaGoolamAriff v. EbrahimGoolamAriff*, (1913) I.L.R. 40 Cal. 1 (P.C.)** – A company was issued the certificate of incorporation by the Registrar on the basis of the Memorandum of Association which was signed by 2 adult persons and by a guardian of the other 5 members who were minors at the time. The guardian signed separately for all the 5 minors. The plaintiff contended that the certificate of incorporation should be declared void. Held, the certificate of incorporation was valid.

After incorporation, the company gets corporate personality. A private company can start business after incorporation. But a public company has to prepare a document called 'prospectus'. After approval by the Registrar of Companies, prospectus is issued to the public. Prospectus is an invitation to the public to subscribe shares. A public company has to secure minimum subscription (minimum capital) within 120 days. Then only certificate of commencement of business is issued by the Registrar. After getting the certificate of commencement of business, a public limited company can start business.

Commencement of business, etc. (Section 11): Section 11 of the Companies Act, 2013, omitted by Act 21 of 2015, w.e.f. 29-5-2015

Registered Office of Company (Section 12): A company; shall, on and from 15th day of its incorporation, and thereafter must be in a position to receive and acknowledge all communication addressed to it.

A verification regarding its registered office shall be filed by the company to the Registrar within 30 days of its incorporation (Section 12(2).

Consequences of not furnishing verification of Registered Office/Notice of change in Registered Office: The

company and every officer, who is in default shall be liable to a penalty of Rs.1,000/- for every day during which the default continues but not exceeding Rs.1,00,000/-. Further, a company having share capital shall not be entitled to commence any business or exercise any borrowing power until it is furnished.

2. Effects/Consequences of Incorporation (Section 9) 'or' Advantages and Disadvantages of Incorporation

The effects or consequences of incorporation may be explained with reference to its advantages and disadvantages.

From the date of incorporation, the company becomes a legal person having perpetual succession and a common seal.

Advantages of Incorporation:

1. Legal Personality.
2. Perpetual Succession.
3. Can sue and be sued.
4. Limited Liability.
5. Transfer of Shares (Sec.44).
6. Separate Property.

1. Legal Personality: After incorporation, a company becomes a legal person, distinct from that of its members. It entirely differs from its members (shareholders). Legal personality of a company was firmly established in 1897 in a leading case, Salmon vs. Salmon & Co.

2. Perpetual succession: The existence of the company continues forever. Death or insolvency or insanity of its individual member does not affect its existence.

3. Can sue and be sued: A company after incorporation becomes competent to sue others and be sued by others. Its officials act on behalf of the company in this regard.

A Company can sue others provided –

i. the act complained is possible to be committed against the company; and

ii. it affects the business or reputation of the company.

Similarly a company can be sued for the acts of its servants (officials) under the principle of vicarious liability, provided

i. the act is committed by its servant; and

ii. such act by servant in discharge of intra vires power.

4. Limited Liability: The liability of the members (shareholders) is limited to the extent of the face value of the shares. Their personal assets are not affected, unless there is an agreement contrary to that effect. E.g: Unlimited Companies (Section 2(92).

5. Transfer of shares (Section 44): The members can freely transfer their shares in an open market without the consent of anybody.

6. Separate property: Being a legal person, a company can own, enjoy and dispose of the property in its own name. The property of the company is different from that of the property of its members.

Disadvantages of Incorporation:

1. Misuse of Corporate veil.
2. Expensive and troublesome.
3. Members ignored from Management.

1. Misuse of Corporate veil: Incorporation confers corporate veil on the company. It distinguishes the company from its members. It gives room for mismanagement, fraud and other irregularities under the shelter of corporate veil.

2. Expensive and Troublesome: Incorporation of a company involves lot of formalities and also expensive. Hence, the promoters engaged in the task of incorporation will face many troubles.

3. Members ignored from Management: Even though the members (shareholders) are the real owners, they are ignored from the Management. The company is managed by a few individuals called 'Directors'.

Among the advantages of the incorporation of a company, corporate personality is of great importance. However, it is subject to misuse by the directors of the company. The misuse of corporate personality can be removed/prevented by lifting the corporate veil. Therefore, corporate personality and lifting or piercing the corporate veil are discussed below in detail.

3. Corporate Personality (Corporate Veil) 'or' the Rule in *Salomon vs. Salomon and Company Limited and Lifting or Piercing the Corporate Veil*

Corporate Personality: After incorporation, a company acquires corporate personality or corporate veil. The word 'veil' denotes a curtain or a shield but not a wall, which parts (separates) the company from its members. In other words, it becomes different from its members. In short, corporate personality, which the company acquires on incorporation, confers legal personality and independent status on the company.

The concept of corporate personality or legal personality was recognised in 1867 in *Oakes v. Turquand and Harding*. But, it was firmly established in a very leading case – Salmon vs. Salmon and Company Ltd.

Salmon v. Salmon and Company Ltd. (1897) AC 22 (1895-99) All ER 33 (H.L):

Facts of the Case: Aron Salomon, a leather and shoe manufacturer sold his business to a company. The company was named Salomon & Company with a share capital of 40000 shares of £ 1 each. The seven subscribers to the Memorandum were Salomon himself, his wife, daughter and four sons. In return for transferring their business, he took 20000 shares and debentures worth of £ 10000. His wife and children owned one share each and the remaining were held by Salomon. After one year, the company went into liquidation. The assets realised were £ 6000 while the liability was debentures held by Salomon £ 10000 and unsecured creditor £ 7000.

An unsecured creditor challenged the right of Salomon to have priority as debenture holder over unsecured creditor. He contended that, though the company was incorporated, it did not have an independent existence on the ground that, the company was nothing but Salomon and his family members. But the court denied the contention and held that, on incorporation, the company became an independent legal person and not an alias or agent of Salomon. Salomon, as a debenture holder was held entitled to get priority in payment over the unsecured creditor.

The Court in the instant case opined that even if one person and his family members contribute to the whole of the capital and have control over the business, yet the members and the company are different persons, separated by corporate veil.

The relevant leading case on this point is –

Lee v. Lee's Air Farming Ltd. (1961) AC 12 – In this case the 3000 shares in Lee's Air Framing Ltd., L held 2999 shares. He voted himself the Managing Director and got himself appointed as chief pilot on a salary. He was killed in an air crash while working for the company. His widow claimed compensation for the death of her husband in the course of his employment. The claim was challenged (at the instance of insurers) that no compensation was due to L as L and Lee's Air Farming Ltd. was the same person. Held, L was a separate person from the company he formed and compensation was due to the widow. 'In effect the magic of corporate personality enabled L to be the master and servant at the same time.'

The Character of a body corporate was explained by the Supreme Court in ***Tata Engineering & Locomotive Co.Ltd. v. State of Bihar* (1964) 34 Comp. Cas. 458 at 468),** as follows:

'The corporation in law is equal to a natural person and has a legal entity of its own. The entity of the corporation is entirely separate from that of its shareholders, it bears its own name and has a seal of its own, its assets are separate and distinct from those of its members, it can sue and be sued exclusively for its own purpose, its creditors

cannot obtain satisfaction from the assets of its members, the liability of the members or shareholders is limited to the capital invested by them, similarly, the creditors of the members have no right to the assets of the corporation'.

In *Naga Brahma Trust v. Translanka Air Travels P.Ltd.*it has been held that shareholders and the company are entirely different persons. Any change in the membership of a company does not mean a change of the company itself.

In India, the corporate personality of an incorporated company has been recognized since 1866 in Re Kondoli Tea Co. Ltd. (1866) ILR 13 Cal. 43.

Advantages of Corporate Personality:

1. Legal Personality.
2. Perpetual Succession (Sec.9).
3. Can sue and be sued.
4. Limited Liability (Sec.9).
5. Transfer of Shares (Sec.44).
6. Separate Property.

1. Legal Personality: After incorporation, a company becomes a legal person, distinct from that of its members. It entirely differs from its members (shareholders). Legal personality of a company was firmly established in 1897 in a leading case, *Salmon vs. Salmon & Co.*

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i. the act is committed by its servant; and

ii. such act by servant in discharge of intra vires power.

4. Limited Liability: The liability of the members (shareholders) is limited to the extent of the face value of the shares, unless there is an agreement contrary to that effect. E.g: Unlimited Companies (Section 2(92)).

5. Transfer of shares: The members can freely transfer their shares in an open market without the consent of anybody.

6. Separate property: Being a legal person, a company can own, enjoy and dispose of the property in its own name. The property of the company is different from that of the property of its members.

Disadvantages (Misuse of Corporate Veil): After registration, the veil of incorporation exists between the company and its members, and company is made distinct from its members. In order to protect themselves from liabilities of the company, its members may take shelter of the corporate veil and may misuse the veil for their selfish ends.

Lifting or Piercing the Corporate Veil (Disregarding Corporate Personality): From the juristic point of view, a company, after registration/ incorporation, is a legal person, distinct from its members. This principle may be referred to as 'the Veil of Incorporation'. The Courts in general bound by this principle. The effect of this principle is that, 'there is a fictional veil and not a wall between the company and its members'. The members/directors, to protect themselves from the liability of the company, may misuse the corporate veil under its shelter. In order to prevent the misuse of corporate veil for unjust and fraudulent acts, it is necessary to lift the veil or disregard corporate personality.

The corporate veil has been lifted by courts and legislatures in the interests of justice, equity and good conscience.

Instances of lifting the corporate veil: Corporate veil may be lifted under the following instances:

1. To prevent fraud or improper conduct;
2. When the company is a mere cloak or sham;
3. Evasion of Tax or avoiding welfare legislation;
4. Under the authority of statute.

1. Fraud and Improper conduct: When the corporate personality is used as an instrument of fraud, the doctrine of piercing the corporate veil may be applied in the interests of justice. Relevant case on the point is:

***P.N.B. Finance Ltd. v. Shital Prasad Jain* (1983) 54 Camp. Cas. 66 –** The defendant was a financial adviser of the plaintiff company. He took loan of 15 lakhs from the company for purchase of some immovable property in Delhi. He did not deposit the title deeds with the company, but diverted the amount to three public limited companies floated by him and his son. In an action against the defendant, his son and three companies, Delhi High Court granted interim relief by lifting corporate veil and directed the defendants to restrain from alienating or disposing of the said properties.

***Jones v. Lipman*(1962) All ER 442 –** L agreed to sell a certain land to J. He subsequently changed his mind and to avoid the specific performance of the contract, he sold it to a company, which was formed specifically for the purpose. The company had L and a clerk of his solicitors as the only members. J brought an action for the specific performance against L and the company. The Court looked to the reality of the situation, ignored the transfer, and ordered that the company should convey the land to J.

2. When the company is a mere cloak or sham (Unlawful act): The corporate veil may be lifted by the courts, where corporate personality is being used as a cloak or sham for doing an unlawful act. Relevant case on this point is :

***Gilford Motor Co. Ltd. v. Horne* (1933) Ch. 935 CA –** The defendant (Horne) was a former employee (M.D) of the plaintiff

company. He had contracted with the Plaintiff Company not to solicit the plaintiff's customers. Contrary to this obligation, he formed a company carrying similar business and dealt with plaintiff's customers. In an action against the defendant, the court granted injunction against the defendant, and his company.

New Horizons Ltd.v. Union of India **(AIR 1994Delhi 126)** – It has been held by the Delhi High Court that not only the Court but even the executive can pierce the veil of corporateness of a company. For example, if a company is black listed by a Government department for some wrongful work, and the directors form another company to obtain a Government contract, the department can pierce the corporate veil to find out who are in fact lurking behind the newly formed company, and thus, deprive the newly formed company to deal with the department.

Tata Engineering and Locomotive Co. Ltd. V. State of Bihar (AIR 1976 SC 2463) – the Supreme Court observed, "where fraud is intended to be prevented, or trading with an energy is sought to be defeated, the veil of corporation is lifted by judicial decisions and the shareholders are held to be persons who actually work for the corporation".

3. Evasion of Tax or avoiding welfare legislation: Corporate veil is lifted by Courts by ignoring the corporate entity/ personality, where corporate personality is misused for evasion of tax or avoiding welfare legislation. Relevant case on this point is:

Sir DinshawManeckjee Petit, Re, **AIR (1927) Bom.** 371 – D, an assessee, who was receiving huge dividend and interest income, transferred his investments to 4 private companies formed for the purpose of reducing his tax liability. These companies transferred the income to D as a pretended loan. Held, the companies were formed by D purely and simply as a means of avoiding tax obligation and the companies were nothing more than the assessee himself. They did no business but were created simply as legal entities to ostensibly receive the dividends and interest and to hand them over to D as pretended loans.

In the instant case, the defendant company diverted the income on investments (dividend on the shares worth of Rs.4,50,000/- of INARCO Ltd.) to its subsidiary Company. Consequently, the bonus of workmen was reduced from 16% to 12%. In an action by workmen against the defendant, the Court held in favour of the workmen.

In ***Bacha F. Guzdar v. C.I.T, Bombay*** **(AIR 1955 SC 74)** – The 60% income of a tea Company was to be considered as agricultural income and was tax free, while 40% of its income was to be considered as income from manufacture and sale of tea, and thus taxable. A shareholder, who received dividend from a tea company, contended that 60% of the dividend should be treated as agricultural income and be exempted from tax. The Supreme Court rejected the contention of the plaintiff on the ground that when the income of the company came to the plaintiff as dividend, it could not be regarded as agricultural income.

4. Statutory Authority: Corporate veil is lifted by the courts if it is necessary or permissible under the statute.

In ***L.I.C. of India v. Escorts Ltd.*** **(AIR 1986 SC 1370 (1986) 59 Comp. Cas. (SC)** – It has been heldthat when the lifting of the corporate veil is necessary or permissible under a certain statute, the courts may do that. But even in such a case the corporate veil may be lifted to that extent and for that purpose only, and no more.

In the **Escorts Case**, under the Foreign Exchange Regulation Act (FERA) and the Portfolio Investment Scheme, non-resident Indians were permitted to invest in Indian companies upto 1% of its paid up equity capital. This facility was also extended to overseas companies in which ownership to the extent of atleast 60% was with the non-resident Indians. In 1983, 13 companies purchased shares of Escorts Ltd. More than 60% of the shares of all these 13 foreign companies were held by a trust of which one person, Mr. Swaraj Paul and the members of his family were the trustees. The Indian Company, Escorts Ltd., questioned the purchase of the shares by the 13 companies. It was contended that they were only 13

companies in name, but only one individual in fact, i.e. Swaraj Paul and his family members only being the beneficiaries in each of the 13 companies, and the limit of investment to the extent of 1% of the paid-up-capital was being circumvented by purchase being made by one person through 13 companies. It insisted on lifting the corporate veil to discover that.

The Supreme Court held that in such a case lifting the corporate veil is necessary and permissible only to find out the nationality or origin of the share holders of the foreign companies seeking to invest in shares of Indian companies.

It was further held that the lifting of the corporate veil could not be done more than as stated above, i.e. there could not be lifting of the veil to find out the individual identity of each of the shareholders. It was, therefore, observed that 'merely because more than 60% of shares of the several foreign companies who have applied for permission are held by a trust of which Mr. Swaraj Paul and the members of his family are the beneficiaries, the companies can be denied the facility of investing in Indian companies.

The Company Act also disregards corporate personality by lifting the corporate veil under the following instances:

i. Reduction of number of members below the minimum.

ii. Fraudulent trading activity by the Company (Section 339).

iii. Holding and subsidiary company: If, the subsidiary company holds corporate personality, the holding company is not liable for the acts of subsidiary company. However, in certain cases, this rule is disregarded by lifting corporate veil.

Further, corporate personality may be ignored by lifting the corporate veil by the Court in times of war, to see whether the company is being controlled by enemy aliens or not, and determine the enemy character of the company by that (*Daimler Co. Ltd. v. Continental Tyre& Rubber Co.* (1916) 2 AC 307 H.L.

4. Promoter and Pre-incorporation Contracts

A) Promoter

Promoter is the person who brings the company in to existence. He attends the entire necessary preliminary work incidental to the formation of a company. In other words, he is the person who takes the necessary steps for formation of the company. The persons, who assume the primary responsibility of matters relating to promotion of a company, are called 'promoters'. After incorporation, the control/management of the company is handed over to the directors called, 'Board of Directors'. The promoters may continue to act as directors in the management of the company. Chronologically, the first persons, who control a company's affairs, are its promoters.

According to the Webster's dictionary, the term 'promoter' includes "a person who alone or with others sets on foot and takes the preliminary steps in the formation of a company". (Webster's Third New International Dictionary, 1971 Ed.).

Lord Cockburn, CJ, in *Twycross v. Grant* [(1877) 2 CPD 469] – observed that "a promoter is a person who undertakes to form a company with reference to a given object and to set it in going and who takes the necessary steps to accomplish that purpose".

As provided in Section 2(69) of the Companies Act, 2013, the term 'Promoter' means a person –

a) Who has been named as such in the prospectus or is identified by the company in the annual return referred to in Section 92; or

b) Who has control over the affairs of the company, directly or indirectly whether as share-holder, director or otherwise; or

c) In accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act:

Provided that nothing in sub-clause (c) shall apply to a person who is acting merely in a professional capacity.

According to Lindley, the term 'promoters' as used in connection with companies, "involves the idea of exertion for the purpose of setting up and starting a company or what is called floating off, and also the idea of some duty towards the company imposed by or arising from the position which the so-called promoter assumed towards it." (*Lindley, J. in Emma Silver Mining Co.Ltd. v Lewis & Son* (1879) 4 CPD 396).

In ***Whaley Bridge Calico Printing Co. v. Green & Smith,* (1880) 5 Q.B.D. 109 –** Bowen L.J. stated that the term 'promoter' is a term not of law, but of business, usefully summing up in a single word a number of business operations familiar to the commercial world, by which a company is generally brought into existence. It is a short and convenient way of designating those who set in motion the machinery by which the Act enables them to create an incorporated company.

In simple words, a promoter is such an important person of the company, who makes untiring efforts to bring the company into existence and strengthens the company to stand on its own feet/ legs.

Position of Promoter: Promoter occupies significant position in formation of a company. However, it is very difficult to determine his accurate legal position, because the company is not in existence. He is neither trustee nor agent of the company. His position may be described with reference to Rights, the following heads namely –

i) Legal Status.

ii) Rights.

iii) Duties.

iv) Liabilities.

i) Legal Status: The Legal position of promoters in relation to the company has been explained by Lord Cairns in *Erlanges v. New Somberero Phosphate Co.* (1878) LR 3 App. Cas. 1218 (1236) – "They (i.e. Promoters) stand in my opinion, undoubtedly in a fiduciary position. They have in their hands the creation and

moulding of the company. They have the power of defining how and when in what shape and under what supervision the prospectus is borne by one of the promoters, he is entitled to recover proportionately from the co-promoters.

As to the exact legal status of a promoter, the statutory provisions are silent in most part, except for a couple of Sections in the Specific Relief Act, 1963. His legal status is incapable of precise statement, but Lindley, L.J. described his position in *Lydney&Wigpool Iron Ore Co. v. Bird*, (1866) 33 Ch.D. 85 as follows:

'Although not an agent for the company, nor a trustee for it before its formation, the old familiar principles of the law of agency and of trusteeship have been extended and very properly extended, to meet such cases.'

Quasi-trustee: A promoter is neither an agent nor a trustee of the company under incorporation but certain fiduciary duties have been imposed on him under the Companies Act, 1956. He is not an agent because there is no principal born by that time and he is not trustee because there is no *cestui que trust* in existence. Hence, he occupies the peculiar position of a quasi-trustee.

ii) Rights: The Promoter of a company is entitled to the following rights –

a) Right to receive/reimburse the preliminary expenses: Preliminary expenses means all the expenses, which are incurred in connection with the registration/incorporation of a company. If the promoter spends from his personal funds during the period of incorporation, he is entitled to recover/reimburse the same. However, the payments made by him should not be ultra vires the articles of association.

b) Right to recover proportionate share from the co-promoters: The liability of promoters is joint and several. In the event of two or more promoters have to meet the liability jointly, and only one promoter meets/clears the liability, he is entitled to recover the proportionate share from the co-promoter/promoters.

iii) Duties:

a) Duty to make no secret profit: A promoter cannot make either directly or indirectly any profits at the expense of the company.

In ***Gluckstein v. Barnes*** **(1900) AC 240** – the promoters were held liable to pay to the company, the unauthorised profit of £ 20000, which they made.

b) Duty to make no profit by sale of his property to the company: He is not allowed to make any profit by sale of his own property to the company, unless all material facts are disclosed.

In ***Erlanger v. N.S. Phosphate Company*** – a person purchased an island, contained mines for £ 55000 and sold the same to the company for £ 110000 to which he was a promoter. It was held that the company could rescind (repudiate) the contract.

c) Duty to make all sincere efforts and prepare required documents for Registration of the Company: He has to take necessary steps for formation of the Company viz. preparation of Memorandum, Articles of Association, prospectus etc.

d) To make a full disclosure of interest or profit: Section 26(1)(a)(xiv) of the Companies Act, 2013 now requires the promoters' earnings to be disclosed in the prospectus itself. It is not the profit by the promoter which the law forbids, but the non-disclosure of it or the non-disclosure of interest in the transaction. If full disclosure is made, the profit is permissible.

The disclosure must be made to an independent Board of directors. Where there is no independent Board, disclosure must be made to the intended shareholders as a whole.

The measure of damages is the actual loss suffered by the company as a result of the transaction in question.

e) The promoter must not make an unfair or unreasonable use of his position and must take care to avoid anything which has the appearance of undue influence or fraud.

iv) Liabilities: Promoter is subject to the following liabilities, preliminary contracts in particular.

1. He is liable for non-compliance of Companies Act (Section 20).
2. He is liable for mis-statements in prospectus (Section 35).
3. He is personally liable for breach of preliminary contracts as enumerated below in detail.

Remuneration of promoters: A promoter has no right to get compensation from the company for his services in promoting the company unless there is a contract to that effect. If there is no such contract, he is not entitled to get any compensation in respect of any payment made by him in connection with the formation of the company.

In re, *National Mail Coach Co.* (1908) 2 Ch. 515 (also known as Clinton's claim) – a syndicate promoted a company and paid £ 416 in respect of fees and stamp duty incidental to the formation of the company. The company afterwards went into liquidation.

It was held that the promoters were not entitled for the payment they had made.

In another case *Re, Rotherham Alum, etc.* (1883) 25 Ch. D. 103) – it was observed that – "It is usual, however, in the Articles of Association to give the Directors power to pay the preliminary expenses out of the company's funds. But such an article gives merely an authority to the Directors to pay such expenses and does not constitute a contract on which the promoter can sue the company".

It is also observed by *Prof. L.C.B. Gower* (Principles of Modern Company Law (1979) Ed. P.332) – "in this respect the promoter is at the mercy of the Directors of the company. But if, as is generally the case, the promoter is one of the Directors, he can be reasonably confident that his expenses will be paid."

However, in *Touche v. Metropolitan Railway Ware Housing Co.* (1871) 6 Ch. Appeals 671) – it has been rightly said by Lord Hatherly – "The services of a promoter are very peculiar, great skill, energy and ingenuity may be employed in constructing a plan and in bringing it out to the best advantage."

In practice, a promoter takes remuneration for his services in one of the following ways:

1. He may sell his own property at a profit to the company for cash or fully paid shares provided he makes a disclosure to this effect.
2. He may be given an option to buy a certain number of shares in the company at par.
3. He may take a commission on the shares sold.
4. The company may pay him a lump sum.

B) Pre-incorporation Contracts (Preliminary Contracts)

Meaning: 'Pre-Incorporation Contracts' means, 'the contracts purported to be made on behalf of the company before its incorporation.' In other words, contracts that were entered into prior to incorporation or during the process of incorporation of a company are called "Pre-Incorporation Contracts" or "Preliminary Contracts". Similarly, expenses incurred in connection the process of incorporation viz. Preliminary Contracts for sale of property, service etc. for incorporation of a company are called 'Preliminary Expenses'.

A Company is not liable to enforce pre-incorporation (preliminary) contracts.

Position of promoters as regards preliminary contracts:

Company not liable: A company, which comes in to existence, is not bound by a preliminary contract through it derived benefit out of the contract. This immunity from liability is accorded on the ground that 'a person is not held liable for the contracts or acts done before his birth'. In the case of –

English & Colonial Produce & Co. Ltd. **(Re (1906) 2 Ch. 435 –** In the instant case, a solicitor prepared Memorandum and Articles and also paid registration fee in consultation with the promoters, (who became directors after incorporation). In an action, the company was held not liable to pay on pre-incorporation contracts.

Company cannot enforce pre-incorporation contract. A Company cannot, after incorporation, enforce the contract made before its incorporation. The leading case on the point is:

Natal Land &Colonisation Co. Ltd. v. Pauline Colliery & Development Syndicate Ltd. **(1904) AC 120** – The N Company agreed with an agent of the P syndicate Ltd. before its formation to grant a mining lease to the Syndicate. The Syndicate was registered and discovered a seam of coal. The Company refused to grant the lease. Held, there was no binding contract between the Company and the Syndicate.

Promoters Liable: The preliminary contracts are deemed to have been entered into personally by the promoters. Hence, the promoters are personally liable in respect of preliminary contracts. The promoters were held personally liable in the case of *Kelner v. Baxter.*

Section 15(h) of the Specific Relief Act, 1963 contains an exception to the above mentioned rule regarding ratification, and permits action by or against the company for specific performance of the contract, if the company accepts the contract. When

i. the promoters of a company have, before its incorporation entered into a contract for the purpose of the company;

ii. such contract is warranted by the terms of the incorporation; and

iii. the company has accepted the contract and has communicated such acceptance to the other party to the contract, specific performance of such a contract may be obtained by the other party to the contract, against the company.

It may be noted that the company's liability under the Specific Relief Act, 1963 arises when the company has taken the benefit under the Contract, but refuses to fulfil its obligation. It does not apply to contract regarding allotment of shares.

The above mentioned provision is applicable both to the public as well as private companies.

5. A Company is not a Citizen

A Company is not a natural person. Hence, it is not a citizen either under the constitution of India, 1950 or under the Citizenship Act 1955. (Heavy Engg. Mazdoor Union vs. State of Bihar, (1969) 39 Comp. Cas. 905).

In ***State Trading Corporation of India Ltd. v. C.T.O.*** **(1963, SC, 1811)** – The Supreme Court held that the S.T.C. though a legal person, was not citizen and could act only through natural persons.

Therefore, the Fundamental Rights guaranteed under Part III of the Constitution are not available to the Company. However, fundamental rights enshrined in the Constitution for protection of 'Person' E.g.: Right to Equality (Art. 14) is available to Company.

In ***R.C.Cooper v. Union of India*****, AIR 1970 SC 564 (Popularly known as Banks Nationalisation Case)** – The Supreme Court held that where a legislation affects the company for which an individual (petitioner) is a shareholder, it affects (infringes) his rights and hence, he can file a petition on behalf of the company under Art.32 of the constitution. Thus, an individual's right is not lost for the reason that he is the shareholder of a company.

A Company has a nationality and residence. Although a company cannot be a citizen, yet it has a nationality, domicile and residence. In *Gasque v. Inland Revenue Commrs.*, (1940) 2 KB 80, Macnaghten J. held:

'It is quite true that a body corporate cannot have a domicile in the same sense as an individual. But by analogy with a natural person the attributes of residence, domicile and nationality can be given to a body corporate.'

In *Tulika v. Parry & Co.* (1903) ILR 27, Mad. 315, Kelly, C.B. observed:

'A joint stock company resides where its place of incorporation is, where the meetings of the whole company or those who represent it are held and where its governing body meets in bodily presence

for the purposes of the company and exercises the powers conferred upon it by Statute and by the Articles of Association'.

Thus a company resides where the central control and management of its business is exercised [*Swedish Central Rly. Co. Ltd. v. Thompson*, (1925) A.C. 495]. Its residence is primarily important in connection with taxation [*United Construction Co. Ltd. v. Bullock*, (1960) A.C. 351].

State of *Gujarat v. Shri Ambica Mills Ltd.* [(1974) 4 SCC 656] – it was held that a citizen shareholder may petition proceeding on behalf of the company against violation of his company's fundamental rights. Further, it has been held that a corporation within the meaning of Section 2(7) of the Companies Act, 1956 a corporation has no fundamental rights as it is not a citizen in terms of Article 5 of Indian Constitution.

As a person, a company can enforce the fundamental rights available to all persons whether citizens or not. It cannot enforce those fundamental rights, which are available to citizens alone. Therefore a company is a legal person, but not a citizen.

Lecture–IV

MEMORANDUM OF ASSOCIATION

This lecture covers –

1. Memorandum of Association: Meaning & Definition.
2. Form of Memorandum.
3. Contents of Memorandum.
4. The Doctrine of Ultra Virus.
5. Alteration of Memorandum of Association.

1. Memorandum of Association: Meaning & Definition

Memorandum of Association is the first and most important document to be submitted to the Registrar for registration of a Company. It contains the relationship between the company and outsiders. It sets out the constitution and foundation on which the entire structure of the company is based. It contains the specific objects for which the company is established. It serves two main purposes namely (1) the shareholders can know, how the funds invested are used/utilized by the company and (2) the outsiders dealing with the company can know exactly the objects of the company and the contractual relation, whom they intend to enter into with the company is within the objects of the company.

'Memorandum of Association' is the document which contains particulars of the specific objects for which a company is established, and covering the whole scope of operation, beyond which it is not legal to go.

'Memorandum of Association of Company' means memorandum of association of a company as originally framed or altered in pursuance of the provisions of the Companies Act.

According to Section 2(56) of the Companies Act, 2013, 'memorandum' means memorandum of association of a company as originally formed or altered from time to time in pursuance of any

previous companies law or of this Act. This definition, however, does not give an idea as to the nature of this document nor it is indicative of its importance.

Lord Cairns in *Ashbury Co. v. Riche* (1875) LR 7 HL 653) observed – "The memorandum defines the limitations of the powers of the company....it contains in it, both that which is affirmative and that which is negative. It states affirmatively the ambit and extent of vitality and powers which by law are given to the corporation, and it states negatively, if it is necessary to state, that nothing shall be done beyond that ambit....."

Lord Macmillan has defined memorandum of association and observed – "it sets out the constitution of the company, it is, so to speak, the charter of the company, and provides foundation on which the structure of the company is built. The importance of the memorandum lies in the fact that it defines the scope of company's activities as well as its relation with the outside world. Its purpose is to enable the shareholders, creditors and those who deal with the company to know what is its permitted range of enterprise."

2. Form of Memorandum (Section 4)

The companies Act prescribes four different forms of Memorandum, which are applicable to different classes of companies and one of these or one as near thereto as circumstances admit has to be adopted (Section 4 of the Companies Act, 2013). Specimen Forms of memorandum for different kinds of companies are set out in Tables A, B, C, D and E in Schedule I as follows:

1. The Form in Table 'A' is applicable in the case of companies limited by shares.
2. The Form in Table 'B' is applicable to companies limited by guarantee and not having share capital.
3. The Form in Table 'C' is applicable to companies limited by guarantee and having a share capital.
4. The Form in Table 'D' is applicable to unlimited companies not having share capital.

5. The Form in Table 'E' is applicable to unlimited companies having share capital.

As far as possible, the company to be incorporated should adopted any of the above mentioned model Forms of memorandum as may be applicable to it, or it may prepare it in any other Form, but the same should be as near thereto as the circumstances may admit. It must be stated that the contents of memorandum shall be valid even though they differ radically from those of the above mentioned models, or even conflict with them. The company may add, subtract or vary the contents thereof so long as the general form of the relevant Table is followed [*Gaiman v. National Association of Mental Health* [(1970) 2 All ER 362].

Any provision in memorandum or articles of a company not having share capital shall not give any right to participate in the divisible profits otherwise than as member of the company.

Printing and signing of Memorandum: The Memorandum of Association of a Company shall be –

a) printed;

b) divided into paragraphs numbered consecutively; and

c) signed by 7 (2 in case of a private company) subscribers.

Each subscriber shall sign (and add his address, description and occupation, if any) in the presence of at least 1 witness who shall attest the signature and shall likewise add his address, description and occupation, if any.

3. Contents of Memorandum (Section-4)

The Memorandum of Association of a company contains the following clauses:

i. Name Clause (Sec.4(1)(2)(3).

ii. Situation or Registered Office Clause.

iii. Objects Clause.

iv. Liability Clause.

v. Capital Clause.

vi. Subscription Clause and

vii. The Association Clause.

i. Name Clause (Sec.4(1)(2)(3)): It contains the name of the proposed company. A company being a legal person must have a name of its own. The name should not be identical (same) to that of a company, which is already in existence. It should not be undesirable in the opinion of the Central Government. The last Word and Words of the name must be 'Limited' in case of a Public Limited Company; and 'Private Limited' in case of a Private Limited Company (Section 4(1)(a)).The name of a Company establishes its identity and is the symbol of its existence.

If a company gets registered with name which resembles the name of an existing company, the other company with whom the name resembles can apply to the Court for an injunction to restrain the new company from adopting the identical name.

In *Asiatic Government Security Life Insurance Co. Ltd. Vs. New Asiatic Insurance Co. Ltd.* [(1939) 9 Comp. Cas. 208] – the names of the two companies resembled to a large extent. It was held by the Court that the two names were not identical, and therefore, the defendants were not restrained from using their name.

Publication of Name by Company: Every company is required to paint or affix its name (and the address of its registered office), outside every office or place in which its business is carried on, shall have its name engraved in legible characters on its seal, if any and shall have its name (and address of its registered office) mentioned in all its business letters and other documents. The Company and its officers who make default in fulfilling this duty are subject to punishment (Section 453).

Change of Name by a Company (Sec.13(2)): A company may change its name only by passing a special resolution and with the written approval of the Central Government. The powers of the Central Government to accord approval to the change of name have been delegated to Registrar of Companies. However, if the change

pertains to only the addition or deletion of the word 'Private' to the name, the approval of the Central Government shall not be necessary.

Proviso to Section 12(3) of the Companies Act, 2013 provides that in case of One Person Company the words 'One Person Company' shall be mentioned in brackets below the name of such company wherever its name is printed, affixed or engraved.

ii. Registered Office Clause (Sec.12): It contains the place and state in which the Registered Office of the proposed company is situated. According to Section 4(1)(b), the memorandum of association should mention the State in which the registered office of the company is to be situated. Section 12(1) envisages that, a company shall have its registered office capable of receiving and acknowledging all its communications from the 30th day of its incorporation. However, the company is not required to furnish the exact address of its registered office. This can be filed with the Registrar of Companies separately in Form INC-22 within 30 days from the date of incorporation of the company or on the day, when it commences business, whichever is earlier so that all communications and notices may be sent to it (Section 12(2)). In practice, the companies file the notice of the address of its registered office at the time of filing the memorandum and articles of association.

Change of Registered Office (Section 12(4) & (5)): In terms of Section 12(4) of the Companies Act, 2013 – 'Notice of every change of the situation of the registered office, verified in the manner prescribed, after the date of incorporation of the company, shall be given to the Registrar within fifteen days of the change, who shall record the same.

By passing special resolution in the company in question can change the situation of its registered office (Section 12(5)).

iii. Objects Clause (Sec.4(1)(c)): The most important clause of the Memorandum of Association is 'the objects clause'. It contains the objects, for which the company is formed. According to Section 4(1)(c) of the Companies Act, 2013, the Memorandum of Association of a Company shall state the objects for which the

company is proposed to be incorporated and any matter considered necessary in furtherance thereof. The objects Clause is divided into three main parts namely –

a) Main objects: This sub-clause contains the main objects to be pursued by the company on its incorporation and objects incidental or ancillary to the attainment of the main objects.

b) Other objects: This sub-clause must include other objects which are not included in the main objects.

c) States to which objects extend: The non-trading companies whose objects are not confined to one State have to state in their object clause, the States to whose territories the objects extend.

However, the Companies Act, 2013 has dispensed with such classification of objects. It only provides –

i) Objects for which the company is proposed to be incorporated and

ii) Any matter considered necessary in furtherance thereof.

The objects enshrined in the memorandum must strictly be complied with. An act beyond these objects is declared as an 'Ultra Vires Act'. An Ultra Vires Act is void (illegal) and cannot be ratified even if all the members wish to ratify it.

Purpose of Objects Clause: The objects clause serves the following purposes –

Firstly, it enables the subscribers to know the use to which their investment money is put and thus extends protection to shareholders.

Secondly, it also extends certain degree of protection to creditors also inasmuch as the company cannot spend its capital on any activities which are not within the purview of the objects clause.

Thirdly, the objects clause also serves the public interest as the company cannot diversity its activities beyond those specified in the objects clause.

In *Crown Bank, Re* [(1890) 44 Ch D 634], the banking company started with the object to act as a bank and further to invest in securities and land and to underwrite issue of securities. The company abandoned its banking business and confined itself to investment and financial speculation. It was held that the company was not entitled to do so.

iv. Liability Clause (Sec.4(1)(d): It contains the nature of liability of its members is limited. Even a company, which is exempted from using the word 'Limited' as part of its name under Section 8 of the Companies Act, 2013 is also required to state in its memorandum that the liability of members is limited. The Memorandum of a company limited by shares or by guarantee shall also state that the liability of its members is limited. This means that the members can only be called upon to pay to the company at any time the uncalled or unpaid amount on the shares held by them, or up to the maximum of the amount which they have guaranteed. On the basis of liability to be met by the members, companies are classified as follows –

i) Company limited by shares (Section 4(1)(d)(i)).

ii) Company limited by guarantee (Section (4)(1)(d)(ii)) and

iii) An unlimited company (Section 2(92)).

i) Company limited by shares (Section 4(1)(d)(i)): In this case, members (share holders) are liable to the extent of shares held by them.

ii) Company limited by guarantee (Section 4(1)(d)(ii)): In case of a company limited by guarantee, the Memorandum of a company must state in the liability clause that each member undertaken to contribute to the assets of the company in the event of its being wound up for payment of debts and liabilities of the company such as may be required not exceeding the specified amount i.e. what he had promised to contribute in formation of a company or in case of winding up of a company.

iii) Unlimited company (Section 2(92)): A company which has no limit on liability, is known as unlimited company. In other words

a company not having any limit on the liability of its members is termed an unlimited company.

v. Capital Clause (Sec.4(1)(e)): It contains the capital structure of the company. The Memorandum of a company, having a share capital, shall state the amount of the share capital with which the company is to be registered and the division thereof into shares of a fixed amount. The capital with which a company is registered is called 'registered', 'authorised' or 'nominal' capital. A Company cannot issue more shares than are authorised for the time being by the Memorandum. The shares issued by a company can only be equity shares or preference shares, but they cannot have disproportionate rights. A private company, which is not a subsidiary of a public company, may issue shares of any kind and with disproportionate rights.

According to Section 4(1)(e) of the Companies Act, 2013 in the case of a company having a share capital – the amount of share capital with which the company; is to be registered and the division thereof into shares of a fixed money and the number of shares which the subscribers to the Memorandum agree to subscribe which shall not be less than one share and number of shares each subscriber to the Memorandum intends to take, indicated Opposite his name. In case of 'one Person Company' the name of the person who in the event of death of the subscriber shall become the member of the company.

In the case of a company limited by guarantee, the amount up to which each member undertakes to contribute-to the assets of the company in the event of its being wound up while he/she is a member or within one year after he/she ceases to be a member for payment of the debts and liabilities of the company or of any such debts and liabilities as may have been contracted before he/she ceases to be a member (Section 4(1)(d)(ii)).

vi. Subscription or Association Clause (Sec.4(1)(e): The Memorandum of Association must be subscribed by at least seven persons in case of a Public Company and two persons in case of private company. Each subscriber must sign the memorandum in the presence of at least one witness.

The subscription or association clause states: 'We, the several persons whose names and addresses are subscribed, are desirous of being formed into a company in pursuance of this Memorandum

of Association, and we respectively agree to take the number of shares in the capital of the company set opposite our respective names.' This is followed by the names, addresses and descriptions of the subscribers and the number of shares taken by each one of them. Each subscriber has to take at least 1 share.

The memorandum shall be signed by at least 7 subscribers in the case of a public company, and by at least 2 subscribers in the case of a private company. The signature of each subscriber shall be attested by at least 1 witness who cannot be any of the other subscribers.

Members severally liable in certain cases (Section 3A): If at any time the number of members of a company is reduced, in the case of a public company, below seven, in the case of a private company, below two, and the company carries on business for more than six months while the number of members is so reduced, every person who is a member of the company during the time that it so carries on business after those six months and is aware of the fact that it is carrying on business with less than seven members or two members, as the case may be, shall be severally liable for the payment of the whole debts of the company contracted during that time, and may also be sued for such acts

4. Doctrine of Ultra Vires or the Rule in *Ashbury Railway Carriage & Iron Co. V. Riche*

A Company has the power to do all such things as are –

1. authorised to be done by the Companies Act, 1956;
2. essential to the attainment of its objects specified in the Memorandum;
3. reasonably and fairly incidental to its objects.

The term 'Ultra' means "beyond", 'vires' means "power or authority". The term 'Ultra vires a company' means "beyond the authority or power" i.e. the doing of an act beyond the legal power and authority of the company.

The persons who subscribe to the capital of the company are to be informed about the objects of the company for which they are paying their money. The object clause in the memorandum, therefore, indicates the purpose for which the company's money is to be used. The object clause serves different purposes. It helps the shareholders

to know for which purpose, their money is utilised. It makes the outsiders to know the extent of the company's powers. It enables the Directors to know within that limit they are authorised to act. Any act beyond the 'Objects Clause' amounts to 'Ultra Vires' act. An Ultra Vires act is void and cannot be ratified even if all the members (shareholders) wish to ratify it unanimously.

The object clause of the company is divided into two sub-clauses namely –

i. Main objects – In this sub-clause must be stated the main objects to be pursued by the company on its incorporation and objects incidental or ancillary to the attainment of the main objects.

ii. Other objects – In this sub-clause must be stated other objects which are not included in the above clause.

The object clause affords a certain degree of protection to the creditors. The creditors of a company give credit not to the shareholders, but to the corporation and they have to seek their repayment out of the company's assets only. The fact that the corporate capital cannot be spent on any project not directly within the terms of the company's objects gives the creditors feeling of security.

The Doctrine of 'Ultra Vires' has been well established in the leading case of: *Ashbury Railway Carriage and Iron Co. Ltd. v. Riche* (1875) LR 7 HL 653

Facts of the case: In the instance case, the Railway company was incorporated with the following objects.

1. To make, sell or give on hire railway carriages and wagons.
2. To carry on the business of mechanical engineers and general contractors; and
3. To purchase, lease, work and sell mines, minerals, land and buildings.

The Directors of the company entered into a contract for financing the construction of a Railway line in Belgium. The company passed a special resolution to ratify the contract. It was held by the

House of Lords that the said contract was Ultra Vires the company and void. The words 'general contractors' did not cover the act, because these words had to be read along with the preceding words, "mechanical engineers" for the purpose of the company's business. It was further held that the contract could not become valid even by the consent (ratification) of all the shareholders.

Lord Cairns observed –

If it was a contract void at its beginning, it was void because the company could not make the contract. If ... every shareholder of the company had said, 'That is a contract, which we desire to make...' the case would not have stood in any different position from that in, which it stands now. The shareholders would thereby, by unanimous consent, have been attempting to do the very thing which, by the Act of Parliament, they were prohibited from doing.

The Doctrine of Ultra Vires as laid down in the Ashbury's case was affirmed (confirmed/further expanded) by the House of Lords in subsequent cases:

Attorney General v. The Great Eastern Rly. Co. **(1880) 5 App. Cas. 473 and** ***London Country Council v. Attorney General*** **(1902) A.C.165.**

Lord Selborne accorded qualified approval to the doctrine.

Deuchar v. Gas Light & Coke Co. **(1925) AC 691 –** A gas company was empowered to make and supply gas, manufacture and sell residuals arising from gas making and to provide such apparatus and materials as it deemed requisite for those purposes. To convert a particular residual, caustic soda was required. After purchasing caustic soda for a number of years, the company decided to manufacture its own caustic soda. Held, it was not ultra vires the company.

Evans v. Brunner Mond& Co. Ltd. **(1921) 1 Ch. 359) –** a company manufacturing chemicals by a resolution authorized its directors to distribute £ 1,00,000 to Universities and Scientific Institutions for the furtherance of scientific research and education. One of the members challenged this act of the company on the ground

that it was ultra vires. The Court held that the distribution of money for scientific research was conducive to the progress of the company as chemical manufacturers and therefore incidental to the company's main objects, hence intra vires and valid.

The doctrine of ultra vires was applied for the first time in India in *Jahangir R. Modi v. ShamijiLadha (1867) 4 Bom. HCR 185)*, where the Bombay High Court held that purchase of a joint stock Company by directors was ultra vires the memorandum of the Company as the Company had not authorized them to enter into such deal.

Effects of Ultra Vires Transactions: The effects or consequences of Ultra Vires transactions may be explained with reference to the following heads:

1. Injunction.
2. Ultra Vires Contracts.
3. Ultra Vires Torts and Crimes.
4. Liability of Directors.
5. Ultra Vires acquired property.
6. Ultra Vires Borrowings.

1. Injunction: If the company has entered into or is about to enter into an ultra vires transaction/act, any shareholder of the company can approach the court for an injunction restraining the company from proceeding with such an ultra vires transaction. *London and County Council v. Attorney General (1902) AC 165*: In this case, the defendant company was authorized to ply tramways as per the objects enshrined in the objects clause. But, contrary to the objects clause, the defendant company plied omni-buses to feed the tramways. The House of Lords held that running of omni-buses was ultra vires and the defendant company was directed by injunction to restrain from running the omni-buses.

2. Ultra Vires Contracts: Ultra Vires Contracts are void ab-initio and not enforceable by or against the Company (*Ashbury Rly. Carriage and Iron Co.Ltd. vs. Riche (1875) LR 7 HL 653).*

In *Re, Beauforte (Jon) (London) Ltd. (1955) Ch. 131*, the objects of the company were to carry on business of costumes and gown making. After the Second World War the company decided to manufacture veneer panels. The court held this activity to be ultra vires. For the purpose of making veneers, the company built a factory at Bristol. A, who built the factory claimed £ 2078, B, who supplied raw materials to the company, claimed £ 1011, C, who supplied coal for use at the factory, claimed £ 107. In the compulsory winding up of the company their claims were rejected by the liquidator as being of ultra vires contracts and the rejection was upheld by the court of chancery. These applicants had no actual knowledge that veneer business was ultra vires, but none of them could make the company liable for their claim.

3. Ultra Vires Torts and Crimes: A Company is held liable for the torts or crimes committed by its officers or directors or servants under the principle of vicarious liability, provided the following conditions are satisfied.

i. The tort or crime has been committed by its Officer/Director/ Servant in the course of employment.

ii. Such act must have been committed within the intra vires powers (i.e. within the objects of Memorandum).

If such torts or crimes come within ultra vires power, the Company is not liable. Relevant case on the point is –

***Poulton v. London and South West Railway* (1867).**

Held in this case that, arrest of a passenger by the defendant Railway servant for non-payment of fare for luggage was ultra vires and the Defendant Company was not liable.

4. Liability of Directors: The liability of Directors may be explained with reference to-

i. towards the Company; and

ii. towards the third party.

i. Towards the Company: If the directors use the funds of the Company for the purpose outside the object clause of the

Memorandum, they will be personally liable to restore such funds to the company (Exchange Banking Co. Re).

In ***A. LakshmanaswamiMudaliar v. L.I.C.*** *(AIR 1963 SC 1185)* – the United India Life Insurance Co. Ltd. was an incorporated company having the principal object of carrying on Life Insurance business. In 1956, the business of the company was taken over by the Life Insurance Corporation of India. In December 1955, shortly before the acquisition, the Directors of company in terms of power vested in the objects clause supported by the resolution of share-holders made a payment of two lakhs rupees as a donation to a trust formed with the object of promoting technical or business knowledge, including knowledge in insurance.

It was held by the Apex Court that the donation of rupees two lakhs was ultra vires and resultantly, the Directors were held personally liable to refund the amount paid to the trust.

ii. Towards the third party: When the directors contract with the third party (on behalf of the company) within the powers of the company and such powers are not contained in the Memorandum, the directors are personally liable (if the third party sues).

5. Ultra Vires Acquired Property: Although ultra vires transactions are void, yet if a company has acquired some property under an ultra vires transaction it has the right to hold that property and protect it against damage by other persons. The property which is legally transferred to the company is in law duly vested in such company even though the company was not empowered to acquire such property, (*National Telephone Co. v. ST. Peter Constables* (1900) AC 317).

6. Ultra Vires Borrowing: Borrowings beyond the object clause of Memorandum are called ultra vires borrowings. In England, such borrowings can be enforced against the company by; the third party, who has acted in good faith. But in India, such borrowings are not enforceable by the lender. However, the lender has certain reliefs in the interests of justice viz. injunction, subrogation etc.

Exceptions of the Doctrine of Ultra Vires:

1. An act which is ultra vires the Directors but intra vires the Articles of Association.
2. An act which is ultra vires the Articles but intra vires the Memorandum of Association.
3. An act which is ultra vires the Memorandum i.e. ultra vires the company itself.

In the first case i.e. where an act is ultra vires the directors but intra vires the Articles that means an act is beyond the authority of the director but within the authority of the Articles then there is no difficulty because the company cannot avoid its liability because the company is liable for such acts by application of doctrine of indoor management and the act of directors can be validated by applying the doctrine of ratification.

In the second case i.e. when an act is ultra vires the Articles of Association but intra vires the memorandum of association which means that an act is against the Articles but it is covered by the memorandum of association then although the company is not bound by such an act and the company can avoid its liability by applying the doctrine of constructive notice, yet to maintain the goodwill of the company, the company can make such transactions binding on it by validating that act by altering the articles of association from retrospective effect and by applying the principle of ratification. Then Company is liable because such an act is permissible within memorandum of association.

But difficulty arises in third case where an act is ultra vires the memorandum of association i.e. beyond the scope and authority of the company itself in other words the act is ultra vires the company. Such acts cannot be validated by altering the memorandum of association. Such acts are not binding on the company and the company is not liable as per doctrine of constructive notice. The act is void.

5. Alteration or Amendment of Memorandum of Association (Section 13)

Alteration or Amendment of Memorandum means changing the contents of Memorandum. E.g. change of name, capital etc. of the company. According to Section 2(3) of the Company's Act, 2013 'alteration' includes 'the making of additions, omissions and substitutions.'

Memorandum of Association may be altered in the following respects:

1. Change of Name (Section 13(2) & 16).
2. Change of Registered Office.
3. Change of Objects Clause.
4. Alteration of Liability Clause.
5. Alteration of Capital Clause (Section 66).

1. Change of Name (Section 13(2) & 16): Change in company's name amounts to 'alteration of its memorandum, which is subject to the provisions enshrined under Section 4(2), (3) of the Companies Act, 2013 and shall not have effect except with the approval of the Central Government in writing. The name of the Company may be changed by special resolution of the shareholders and with the approval of Central Government signified in writing. If the name, in the opinion of the Central Government is identical with, or too nearly resembles, the name can be altered by the ordinary resolution of the shareholders with the previous approval of the Central Government (Sec.16). When the name is altered, the Registrar of Stock Companies shall issue a fresh certificate of Registration/Incorporation to that effect Section 13(3). Rights and obligations remain unaffected. The change of name shall not affect any rights or obligations of the company, or render defective any legal proceedings by or against the company. Legal proceedings which might have been continued or commenced by or against the company by its former name may now be continued by its new name. This is because the alteration is only in name and not in the

identity of the company [Kalipada vs. Mahalaxmi Bank Ltd. AIR (1966) Cal. 585].

2. Change of Registered Office (Sec.13(4)): No company shall change the place of its Registered Office from one place to another within the State unless such change is confirmed by the Regional Director. For the purpose of shifting the Registered Office one place to another within the same State, a special resolution should be passed and a notice to that effect should be issued/served to the Registrar of Companies within its jurisdiction within 30 days (Section 12(6).

In case a company proposed to shift its registered office from one State to another, it has to alter its memorandum of association subject to compliance of the provisions of Section 13 of the Companies Act, 2013 which require passing of a special resolution and approval of the Central Government. The alteration relating to change of the place of its registered office from one State to another shall not take effect unless it is confirmed by the Central Government on petition.

The Central Government shall also give a reasonable opportunity to every person on whom the notice of alteration is served to appear before it and put-up his objections, if any. Thereafter, the Central Government may make an order confirming the alteration on such terms and conditions, if any, with respect to the confirmation of the alteration. It may, for the purpose of the interests of dissenting members, give such directions and make such orders as it thinks fit for facilitating or carrying into effect, any such alteration.

The alteration shall be registered within sixty days from date of its confirmation by the Central Government. On receipt of the confirmation by the Central Government, the Company shall file with the Registrar a copy of the special resolution passed by the company along with a certified copy of the order of the Central Government confirming the alteration together with a printed copy of the memorandum as altered and the Registrar shall register the same and certify the registration under his hand within thirty days month from the date of filing of such document.

A Company may, by special resolutions, change the place of Registered Office from one state to another for certain purposes. The alteration is subject to confirmation by the Central Government on an application in such form and manner as prescribed (Section 13(4).

3. Change of Objects Clause: The objects clause of a company comprises of three parts, namely —

i. Main objects.

ii. Other objects, and

iii. The states to whose territories the objects extend.

Before the amendment of the Companies Act in 1956, alteration of the 'objects clause' in the Memorandum of a company required approval of its shareholders by a special resolution and confirmation of the same by the Company Law Board. The Amendment Act, 1996 seeks to remove the requirement of confirmation of change by the Company Law Board. As a result, a company would be free to amend the 'objects clause' with the approval of its shareholders.

Now, the objects clause of a company can be amended –

i) By passing a special resolution to that effect by share-holders, and

ii) By serving/issuing a notice (or filing a copy) to that effect to the Registrar of Companies within one month.

A Company by special resolution may alter the objects clause for the following purposes:

i. To carry on business more economically and efficiently; or

ii. To attain its purpose by improved means; or

iii. To enlarge or change its local area of operation; or

iv. To carry on some business, which can be combined with the business of the company; or

v. To restrict or abandon any of the objects; or

vi. To sell or dispose of the whole or any part of the undertaking of the company; or

vii. To amalgamate with any other company; or body Corporate or persons.

Procedure for Alteration of the Objects Clause: An alteration in the objects clause of a company shall not have any effect until special resolution has been passed by the shareholders of the company for this purpose and is confirmed by the Central Government. The Central Government is, however, free to confirm the alteration wholly or in part, and it can even refuse to confirm it on reasonable grounds. However, before confirming the alteration, the Central Government must be satisfied that –

a) sufficient notice has been given to every debenture-holder (i.e. creditor) of the company and to persons whose interests are likely to be affected by the alteration, and

b) the objections to the proposed alteration of objects, if any, have been properly disposed of to the satisfaction of the Central Government.

The Central Government must also send as notice of alteration to the Registrar of Companies to enable him to appear before the Board and file objections, if any, in respect to confirmation of alteration.

The Central Government may choose to impose reasonable conditions while confirming the alteration of the memorandum of a company. The change in the objects clause may also require a consequential change in the company's name so as to indicate the change in the character of business of the company (In *Re Standard General Assurance Co. Ltd.* AIR 1965 Cal. 16).

The State Government may object to a change in the capacity of a creditor in respect of the arrears of revenue due to it from the company.

4. Alteration of liability clause: A company cannot alter the liability clause of the Memorandum of Association so as to enhance the liability of its members or compelling them to take further shares. However, it can alter the Memorandum in the following cases:

i. When members agree in writing (before or after such alteration is made);

ii. Where the Company is a club or association.

5. Alteration of capital clause (Sec.61): Section 61 of the Companies Act, 2013, provides for the 'alteration of capital clause' if authorized by its articles of association for the following purposes:

i) to increase its share capital by issue of new shares (Sec.4(1)(d).

ii) to consolidate existing shares of larger denomination (Section 61(1)(b).

iii) to sub-divide its shares or any of them into shares of smaller amount than is fixed by memorandum (Section 61(1)(d).

iv) to convert fully-paid shares into stock or vice versa (Section 61(1)(c).

v) to cancel unissued shares and to that extent diminish the amount of its shares capital. Such cancellation shall not, however, be deemed as reduction of share capital (Section 61(1)(e).

For the purpose of alteration of the share capital, if authorized by the articles of association, a resolution to that effect should be passed by the general meeting and the resolution must be filed with the Registrar of Companies within 30 days. Then the Registrar of Companies records such changes (alteration) in the Companies' memorandum or articles or both. In case the proposed alteration is to reduce the capital, which the company finds in excess, strict procedure under Section 66 must be adhered to. Section 66 envisages special resolution by the share-holders and a petition to that effect should be filed in an appropriate Tribunal for confirmation.

Provided that no consolidation and division which results in changes in the voting percentage of shareholders shall take effect unless it is approved by the Tribunal on an application made in the prescribed manner.

Lecture–V
ARTICLES OF ASSOCIATION

This lecture covers –

1. Articles of Association: Meaning, Definition and Nature.
2. Form of Articles of Association.
3. Contents of Articles of Association.
4. The Doctrine of Constructive Notice and The Doctrine of Indoor Management or The Rule in Royal British Bank v. Turquand or Doctrine of indoor management is a Sliver Line to the Strangers.
5. Alternation or Amendment of Articles of Association, and
6. The Distinction between the Memorandum of Association and Articles of Association.

1. Articles of Association: Meaning, Definition and Nature

Meaning: Memorandum of Association and Articles of Association are the two important documents, to be filed with the Registrar of Companies for incorporation/registration of a company. The former (memorandum) contains the relationship with the company and outsiders/public, while the latter (Articles) contains the internal relationship between the company and its members, directors inter se and conduct of the company's business.

Thus, the second and the most important document to be submitted to the Registrar of Companies is the "Articles of Association". It contains the rules, regulations and byelaws for successful conduct and smooth running of the company. In simple words, it is the charter of the company to carry out its objects enshrined in the Memorandum of Association.

'Articles of Association' is a written agreement prescribing regulations for the government of a company. 'Articles of Association' or 'Articles of incorporation', the certificate filed, in conformity with

law by persons who desired to become a corporation and setting forth the rules and conditions upon which the association or corporation is founded.

Definition and Nature: Section 2(5) of the Companies Act, 2013, defines 'Articles of Association' as "Articles means the articles of association of a company as originally framed or as altered from time to time or applied in pursuance of any previous companies' law or of this Act."

Lord Cairns L.C. described the functions of Articles of Association of a company in *Ashbury Railway Carriage & Iron Co. Ltd. v. Riche* (1875) LR 7 HL 653) – "The articles play a part subsidiary to the memorandum of association. They accept the memorandum as the charter of incorporation of the company, and so accepting it, the articles proceed to define the duties, rights and powers of governing body as between themselves and the company at large, and the mode and form in which business of the company is to be carried on, and the mode and form in which changes in internal regulations of company may from time to time be made....."

As stated above, memorandum of association lays down the scope and powers of the company while the articles of association govern the ways in which the objects enshrined in memorandum of the company are to be carried out/achieved. In case of a conflict between the provisions of memorandum and articles, the provisions of the memorandum will prevail over the articles.

2. Form of Articles of Association

Articles of Association shall be in a specified form as prescribed tables F, G, H, I and J in Schedule I of the Companies Act, 2013.

Table F – Articles of Association of a company limited by shares, deals with share capital and variation of rights, lien calls on shares, Transfer of shares, Transmission of shares, Forfeiture of shares, Alteration of capital, Capitalisation of profits, Buy-back of shares, General meetings, proceedings of general meetings, Adjournment of meetings, Voting rights, Proxy, Board of Directors, Proceedings of the Board, The seal, Dividends and Reserve, Accounts, winding up and Indemnity.

Table G – Articles of Association of a company limited by guarantee and having a share capital.

Table H — Articles of Association of a company limited by guarantee and not having share capital – which deals with members, General meetings, adjournment of meeting, voting rights, Board of Directors, Proceedings of the Board, and Chief Executive Officer, Manager, Company Secretary or Chief Finance Officer.

Table I – Articles of Association of an unlimited company and not having share capital.

Table J – Articles of Association of an unlimited company and not having share capital. By virtue of Section 5(7) a company may adopt all or any of the regulations contained in the model articles, applicable to such company.

Form and Signature of Articles : The Articles shall be –

a) Printed.

b) Divided into paragraphs and

c) Signed by each subscriber of the Memorandum (who shall add his address, description and occupation, if any) in the presence of at least 1 witness who will attest the signature and likewise and his address, description and occupation, if any.

The Articles of Association printed on computer laser printer should be accepted by the Registrar for registration of a company provided they are neatly and legibly printed (Press Note, issued by the Department of Company Affairs, dated 22-6-1993),

3. Contents of Articles of Association

Articles of Association regulate the internal management of the Company. Section 5 of the Companies Act, 2013 declares that the Articles of a company shall contain regulations for management of the company. The contents of the Articles of Association closely correspond to the matters enshrined/enlisted in Table F of the Schedule I of the Companies Act, 2013. It contains the following:

i) Exclusion wholly or in part of Table F.

ii) Approval of Preliminary Contracts.

iii) Capital Rights and their variations.

iv) Share capital: Number and Kinds of Shares, their face value, issue and allotment, called up, paid up etc.

v) Lien on Members' shares.

vi) Transfer and Transmission of shares.

vii) Alteration of Share Capital.

viii) Forfeiture of shares.

ix) General meetings, Special Meetings, Voting, Proxies etc.

x) Directors, their qualification, appointment, powers, duties, remuneration etc.

xi) Secretary, his appointment and remuneration.

xii) Borrowing powers.

xiii) Dividends and Reserves.

xiv) Accounts and Audit.

xv) Winding up, powers of Liquidator and

xvi) Indemnification of officers out of assets of the company.

4. The Doctrine of Constructive Notice and the Doctrine of Indoor Management or the Rule in *Royal British Bank Vs. Urquand or Doctrine of Indoor Management is a Sliver Line to the Strangers*

Memorandum of Association and Articles of Association are the most important documents to be submitted for incorporation of a company. They are the public documents. Memorandum contains the relationship between the company and outsiders, while the Articles contains the constitution and internal management of the company.

Constructive Notice: Memorandum and Articles are public documents and are open to the public for inspection. These documents are available in the office of the Registrar of Companies (Section 399, Companies Act, 2013) and a copy of the same can

be obtained by payment of a prescribed fee. In other words, once the memorandum and articles are registered in the office of the Registrar of Companies, all the persons, who wish to deal/contract with the company, shall be presumed to have the knowledge or notice as to the contents of the memorandum and articles. Such knowledge or notice is called 'Constructive Notice'.

Any person who has contracted with the company cannot plead subsequently that he did not have knowledge or notice as to the contents of these documents. Before contracting, he must make sure that his contract is consistent with these documents. The person dealing with the company is bound by the law of estoppel, and he cannot be allowed to say that he had no actual notice of the contents of these documents.

The doctrine of constructive notice applies not only to Memorandum and Articles, but also the other documents, which have to be filed with the Registrar, such as special resolutions, and particulars of changes.

Section 398 of the Companies Act, 2013 provides that applications, documents, for inspection etc. Filed in the electronic form shall be accepted and maintained by the Registrar in the manner prescribed.

The Central Government may, by notification, frame a scheme to carry out the provisions of sub-section (1) of Section 398 through the electronic forming.

It may be noted that a person dealing with the company is taken to have not only read the documents but also to have understood their proper meaning.

In ***KotlaVenkataswamy v. Ram Murthy,*** **(AIR 1934 Mad. 579),** the Articles of Association of a Company stipulated that a deed on behalf of the company should be signed by three specified officers, viz. the Managing Director, the Secretary and a Working Director. The plaintiff accepted a mortgage deed, which was, signed by two officers only, i.e. the Secretary and Working Director.

It was held that the said mortgage deed was invalid, and the plaintiff could not claim any rights under it. The reason for the decision was that if the plaintiff had consulted the Articles she could have known that the deed needed signatures of three specified officers. The fact that the plaintiff had acted in good faith, and her money had been utilised by the company could not change the position.

Unreal Doctrine: The Doctrine of constructive notice is subject to criticism as an unreal doctrine and it protects the interest of the company at the cost of an innocent outsider for the simple reason, he/she is ignorant of the contents of the memorandum and articles protect the company. It is an Unreal Doctrine, since it fails to take note of realities of business life.

According to Palmer, the doctrine of the constructive notice applies to all such documents of the Company which affect its powers. But from the practical stand point, this view appears to be unrealistic because people know about the Company through its officials and not its documents. The rule has therefore, been abandoned in Europe (Section 9(i) of the European Communities Act, 1972).

The doctrine of 'Constructive Notice' is subject to restrictive operation by –

A) The Doctrine of Indoor Management; and

B) The Doctrine of Holding out.

A) The Doctrine of Indoor Management: The doctrine of indoor management constitutes an exception to the principle of constructive notice. The doctrine of constructive notice is based on the fact that the memorandum and articles, being public documents, their contents are supposed to be known to everyone dealing with the company. The doctrine of indoor management relates to the internal matters, and an outsider can presume that the internal working of the company is in consonance with the provisions of public documents. He need not enquire into the regularity of the internal proceedings.

This doctrine restricts the operation of constructive notice and protects the outsider. According to this doctrine, when the Articles of Association prescribes a particular procedure for a particular thing, the duty to comply with such procedure lies on the person in charge of Management of the Company. The person (outsider) dealing with the company is not bound to enquire about the irregularity of the internal proceedings.

The outsider dealing with the company is presumed to know the constitution of the Company and is not expected to know what takes place within the doors that are closed to him.

This view was laid down in 1856 in a leading case of –

Royal British Bank v. Turquand[(1856) 6 E & B 327] and hence, it ispopularly known as *'The Rule in Royal British Bank v. Turquand'*.

Facts of the case: The Directors of the Defendant Company borrowed money from the plaintiff (Turquand). According to Articles of Association, the Directors have borrowing power subject to authorisation by shareholders' resolution. The plaintiff's claim was denied on the ground that there was no resolution by shareholders to that effect. However, the court denied the contents of the shareholders and held the company liable.

This rule laid down in the above case is based on public convenience and justice.

Instances: The Doctrine of Indoor Management is applicable in the following situations.

1. Where Directors' title to office is defective.
2. Failure to convene Board meetings properly; and
3. Disregard of limitations on the Directors' authority.

Exceptions: The Doctrine of Indoor Management is not applicable to the following.

1. Void Acts: The protection under this doctrine is not available to the outsider, if the contract entered into is void *ab initio*. E.g: Forgery Act. Another exception to the doctrine of 'Indoor

Management' where the acts done in the name of the company are void ab initio due to forgery or fraud. The decision in *Ruben v. Great Fingall Consolidated* (1996) AC 469) illustrates this exception well. In this case the Secretary of a company forged the signatures of two directors required under the articles on a share certificate and issued the same without authority. The plaintiff who was the transferee of the share certificate contended that whether the signatures were genuine or forged was something pertaining to internal management of the company and, therefore, the company should be stopped from denying the genuineness of the certificate.

2. Knowledge as to Irregularity: If the person had full knowledge (at the time of contract) as to the internal irregularities of the company, he cannot claim protection under the doctrine.

In *Howard v. Patent Ivory Manufacturing Co.* (1888) 38 Ch.D. 156) – the directors had no power to borrow money more than £12,500 from themselves and look debenture without obtaining the sanction of the general meeting, it was held that they ;had the notice of internal irregularity and therefore the debenture only to the extent of £11,000 were held valid.

In *Devi Ditta Mal v. The Standard Bank of India* (1927) 101 IC 568) – the transfer of shares was approved by two directors, one of whom within the knowledge of the transferor was disqualified by reason of being the trustee himself and the other was never validly appointed. The transfer, was, therefore, held invalid and without any effect.

In *Morris v. Kanssen* (1946) AC 459) – a director could not defend an allotment of shares to himself as he participated in the meeting which made the allotment and his appointment as director was also not in order because none of the directors appointing him were validly in office. Thus it is clear that where a person who is himself a part of the internal machinery of a company, cannot be allowed to take advantage of irregularity.

3. Negligence: If the person (outsider) negligently did not enquire as to the irregularities he cannot plead/invoke the defence under the doctrine.

4. Ignorance of Articles: A person who does not have the knowledge of Articles of Association cannot claim protection under this doctrine.

In *Lakshmi Rattan Lal Cotton Mills v. J.K.Jute Mills Co.* (AIR 1957 All. 311) – in this case 'G' was the director of a company. The company had managing agents whose director was also 'G'. The Articles authorized the directors to borrow money and also empowered them to delegate this power to any other director or directors. 'G' borrowed money from the plaintiff. The company refused to be bound by the loan on the plea that there was no resolution as to delegation of power to 'G'. However, the Court held the company liable. The reason being that even if there was no actual resolution authorizing 'G' to enter into transactions, the plaintiff was right in assuming that the power which could have been delegated under the articles must have been actually conferred in fact.

B) Doctrine of Holding out: The doctrine of holding out creates an exception to the doctrine of constructive notice. If a person is held out by the company as its officer, the act of the person falling within the actual or ostensible authority of the officer will be binding on the company. It is based on the Doctrine of Estoppel. The expression 'estoppel' is derived from the French word 'estoup', which means, "shut the mouth". It is based on the principle of equity and good conscience. It (estoppel) is enshrined in the Latin maxim 'Alleganscontrariaaudierdus', which means, "a man alleging contradictory facts ought not to be heard". The object of the principle of estoppel is to prevent fraud and to manifest good faith among the parties. Holding out is a breach of the principle of estoppel. E.g.: 'A' is held out as a Manager of a company, but he is not so in reality. Later, the Company cannot deny his acts under the authority as Manager. Similarly, 'A' is the owner of a T.V.Show Room. 'A's friend, 'B' visits the shop now and then. 'A' allows 'B', actively involved in the business transactions so that the customers/outsiders presumed 'B' as the Managing Partner. Then 'B' is the Partner by holdingout. 'A' cannot deny any payment made to 'B' by the customers and 'A' is liable for the same.

Thus, if the company represents that a person is an officer of the company, it cannot be allowed to say that he is not its officer and the act of the officer will be binding on the company. The doctrine of holding out is based on the doctrine of estoppel, which says that a person cannot be allowed to deny the truth of his statement.

In the case of ***Freeman & Lockyer v. Buckhurst Park Properties (Mangal) Ltd.*** the court has held that a contractor can hold the company liable for a contract made on its behalf on the ground of holding out if the following are proved:

1. That a presentation that the agent or the officer had authority to enter, on behalf of the company, into a contract of the kind sought to be enforced was made to the contractor.
2. That such representation was made by a person or persons who had actual authority to manage the business of the company either generally or in respect of those matters to which the contract relates.
3. That he (the contractor) was included by such representation to enter into the contract, that is, that he in fact relied upon it; and
4. That under its memorandum or articles the company was not deprived of the capacity either to enter into a contract of the kind sought to be enforced or to delegate authority to enter into a contract of that kind to the agent.

It is clear from the above that, the doctrine of constructive notice protects the company against outsiders, whereas, the doctrines of indoor management and holding out seek to protect outsiders against the company.

5. Alteration of Articles of Association (Sec. 14)

According to Section 14 of the Companies Act, 2013, a company has a statutory power to alter its Articles of Association by special resolution. The power to alter is subject to the conditions contained in the Memorandum. Such alteration is binding on every member of the company and no member shall object it. The Articles

must be altered in good faith. The word 'alteration' includes additions and omissions.

Section 14 runs as follows:

Subject to the provisions of this Act and the conditions contained in its memorandum, if any, a company may, by a special resolution, alter its articles including alterations having the effect of conversion of-

a) A private company into a public company, or

b) A public company into a private company.

Provided that where a company being a private company alters its articles in such amanner that they no longer include the restrictions and limitations which are required to be included in the articles of a private company under this Act, the company shall, as from the date of such alterations, cease to be a private company.

Provided further that any alteration having the effect of conversion of a public company into a private company shall not be valid unless it is approved by an order of the Central Government on an application made in such form and manner as may be prescribed:

Provided also that any application pending before the Tribunal, as on the date of commencement of the Companies (Amendment) Act, 2019, shall be disposed of by the Tribunal in accordance with the provisions applicable to it before such commencement.

Every alteration of the articles under this section and a copy of the order of the Tribunal approving the alteration as per sub-section (1) shall be filed with the Registrar, together with a printed copy of the altered articles, within a period of fifteen days in such manner as may be prescribed, who shall register the same.

Any alteration of the articles registered under sub-section (2) shall, subject to the provisions of this Act, be valid as if it were originally in the articles.

Procedure for Alteration of Articles:

1. The proposed alteration is to be placed before the Board ofDirectors for approval. The Board shall decide the date and time of the General meeting. The Secretary is authorized to convene the meeting.

The Board will also approve the draft of notice, special resolution and explanatory statement. If the alteration requires taking or subscribing more shares by the members than already held by them, prior consent of the members in writing shall be necessary before passing the special resolution to this effect.

2. On the appointed day, the meeting will be held to pass the special resolution.

3. Within 30 days of such resolution, Form No.MGT-14, with prescribed fee has to be filed with the Registrar along with certified copy of the resolution.

4. If the alteration is to convert public company into private company, the company within three months of special resolution, should file an application in writing in Form No.1.B with the Regional Director of Companies concerned for approval.

5. After approval, a printed copy of the Articles as altered shall be filed with the Registrar of Companies within 15 days from the date of receipt of the approval order (Section 14(2).

6. In case the shares of the company are listed on a Stock Exchange as per SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, the Company must forward to the Exchange, the copies of all notices sent to its shareholders.

7. The alteration should be noted on each copy of the articles of association.

Limitations on the power to alter Articles:

A Company may alter its articles by passing special resolution (in general meeting) subject to the following restrictions:

1. The alteration must not exceed the powers, conferred under the Memorandum of Association (i.e. intra vires). In case of conflict between the Memorandum and Articles, Memo will prevail.

2. The alteration must not be inconsistent with any of the provisions of the Companies Act or any other Statute.

3. The alteration must not be illegal or opposed to public policy.

4. An alteration for breach of contract is not justified (*Southern Foundries Ltd. v. Shirlaw*).

5. Any alteration in the Articles which tends to increase the liability of a member to contribute more than his share-holding is not binding on him, unless he consents to it in writing.

6. A company cannot justify a breach of contract with other parties by altering its articles. It shall remain liable for damages for its breach. (*Southern Foundries Ltd. v. Shirlaw* 1940 AC 701.

7. A reserved liability once created cannot be converted into unreserved liability by altering the articles but it may be cancelled on a reduction of capital.

8. The alteration must not be inconsistent with the order of the National Company Law Tribunal.

9. An alteration must not constitute a fraud on the minority nor should it cause any hardship on the minority without any corresponding benefit to the Company as a whole.

6. The Relation or Distinction between the Memorandum and Articles

Memorandum of Association and Articles of Association are the most important documents to be submitted to the Registrar of Companies for incorporation of a company. Memorandum of Association contains the relationship between the company and outsiders. It enables the outside world, the shareholders, the creditors and others, to know about certain vital aspects about the company, with which they are dealing. Where as, the Articles of Association is a document, which contains the constitution of the Company. It lays down the rules and regulations for the administration of the Company.

Following are the notable points of distinction between The Memorandum and Articles.

Memorandum of Association	Articles of Association
1. It is the fundamental or the first and foremost important document of the Company.	1. It is the subsidiary document. Articles are subordinate to Memorandum.
2. It is the charter of the Company indicating the nature of its business, its nationality and its capital.	2. It contains rules and regulations as to internal management of the company as set out in the Memorandum.
3. It defines the Company's relationship with outside world.	3. It defines the Company's relationship with inside world i.e. internal management.
4. It cannot be altered so easily.	4. Articles can be altered easily by special resolution of the shareholders in the General Meeting.
5. Any act of the company, which is ultra vires, the Memorandum is wholly void and cannot be ratified even by the whole body of shareholders.	5. Any act of the company, which is ultra vires, the Articles (but is intra vires the Memorandum) can be confirmed by the shareholders.
6. In the event of conflict/ dispute, Memorandum supercedes the Articles.	6. In the event of conflict between the Memorandum and Articles, articles should give way to the Memorandum.

As stated above, Articles of Association is subordinate to the Memorandum. In the event of conflict between the provision of Memorandum and the provision of Articles, the provision of Memorandum will prevail over the provision of the Article.

In *Bryon v. Metropolitan Ombibus Co.* [(1885) 27 LJ Ch. 685] it was observed that 'this is so because the object of the Memorandum is to state the purposes for which the company has been established, while the Articles provide the manner in which the company is to be carried on and its proceedings disposed of.' This is the main difference between the two documents.

Lecture–VI
PROSPECTUS

Chapter III of the Companies Act, 2013 lays down the provisions relating to "Prospectus and Allotment of Shares". It comprises of two parts namely, Part I containing Sections 23 to 41 deals with the provisions relating to Public Officer, while Part II containing Section 42 deals with "Private Placement".

This lecture covers –

1. Prospectus: Meaning and Definition.
2. Registration of Prospectus.
3. Objects of Prospectus.
4. Characteristics of Prospectus.
5. Contents of Prospectus.
6. When Prospectus need not be Issued.
7. Deemed Prospectus (Sec.25).
8. Shelf Prospectus (Sec.31).
9. Red Herring Prospectus (Sec.32).
10. Misstatement of Prospectus (The Golden Rule).
11. Underwriting Commission and Brokerage.
12. Allotment of Securities by Company (Sec.39) and
13. Prospectus of Foreign Companies (Sec.387).

1. Prospectus: Meaning & Definition: Prospectus is an important document to be submitted to the Registrar of Companies after incorporation of Public Limited Company. 'Prospectus' is an "Invitation to the public to offer to subscribe shares". After incorporation (registration) a public limited company has to secure minimum subscription (capital). According to Section 25 of the Companies Act, 2013, "no application for shares or debentures of a company can be invited/entertained unless the appeal/requisition is accompanied with a prospectus.

A public company may issue securities to public through public offer which is referred to as Prospectus (Section 23(1) of Companies Act, 2013). A private company may issue securities by way of rights issue or bonus issue to the existing share-holders.(Section 23(2)).

L.B. (Curzon), "Prospectus" means, 'any document containing information about securities.' However, literally expression "Prospectus" means 'a circular of the chief features of an enterprise, school books, etc.'

Tophan defined the term prospectus in his words – "A prospectus is usually a circular or newspaper advertisement published by the promoters after the formation of the company to induce the public to take shares in the company."

As per Section 2(70) of the Companies Act, 2013, "Prospectus" means 'any document described or issued as a prospectus and includes a red herring prospectus referred to in Section 32 or shelf prospectus referred to in Section 31 or any notice, circular, advertisement or other document inviting offers from the public for the subscription or purchase of any securities of a body corporate.

The word 'subscription' in the definition of prospectus means 'taking' or 'agreeing to take' shares for each. It imports that the person agreeing to take the shares puts himself under a liability to pay the nominal amount thereof in cash [*Govts. Stock & Other Securities Investment Co. Ltd. v. Christopher*, (1956) All ER 490].

Any advertisement inviting the public for purchase of shares or debentures of the company is called "Prospectus".

In *ParamathaNathSanyal v. Kali Kumar Dutt* [AIR 1925 Cal. 714], an advertisement was given in a newspaper stating: "Some share are still available for sale according to the terms of the prospectus of the company which can be obtained on application". It was held to be a prospectus as it invited the public to purchase shares.

A prospectus must be in writing. An oral invitation to subscribe for shares in, or debentures of, a company, or deposits is not a prospectus. Likewise, an advertisement in television or a film is not treated to be a prospectus.

2. Registration of prospectus (Sections 27(7)): A prospectus issued by or on behalf of a company or in relation to an intended company shall be dated. That date shall be taken as the date of publication of the prospectus, unless the contrary is proved.

A prospectus can be issued by or on behalf of a company only when a copy thereof has been delivered to the Registrar for registration. The registration must be made on or before the date of publication thereof. The copy must be signed by every person who is named therein as director or proposed director of the company, or by his agent authorised in writing. Further such a prospectus must state on the face of it that a copy of it has been delivered to the Registrar for registration on or before the date of its publication. It must accompany the following documents:—

a) The consent of the expert, if his report is to be published in the prospectus.

b) A copy of every contract relating to the appointment or remuneration of managerial personnel.

c) A copy of every material contract not being a contract entered into in the ordinary course of business of the company into within two years of the date of issue of prospectus.

d) A written statement

e) The consent in writing of the person, if any, named in the prospectus as auditor, Legal Adviser, Attorney, Solicitor, Issue House banker or broker of the company to act in that capacity.

f) The consent of director in respect of new directors, if any, named therein.

g) A copy of the underwriting agreement, if any, should also be filed along with the prospectus.

Statement in lieu of prospectus: Section 70 of the Companies Act, 1956 provided that the statement in lieu of prospectus should be delivered to the Registrar in certain cases. However this provision of statement in lieu of prospectus has been omitted in Companies Act, 2013.

3. Objects of Prospectus: The objects of prospectus are as follows –

i) To bring to the notice of the public that a new company has been formed.

ii) To arouse interest of the public to make investment in the company.

iii) To create confidence in the public about the company, its directors and its profitability, and

iv) To secure that the directors of the company accept responsibility of the statements in prospectus.

4. Characteristics of Prospectus:

i) Prospectus to be in writing:- A prospectus must be in writing. An oral invitation or advertisement in T.V. and film is not treated to be a prospectus.

ii) Invitation for the subscription:- The word 'subscription' means 'taking' or 'agreeing to take' shares for cash. Prospectus invites the public to subscribe for shares in, or debentures of, a company.

iii) Public Issue:- 'Public' means 'the people'; 'the general body of mankind'; 'of or belonging to the people';

'the body of the people at large'. 'Public includes any class of the public or any community'.

5. Contents of Prospectus (Section 26)

Section 26 of the Companies Act, 2013 provides for the matters/contents to be furnished in the prospectus. It runs as follows:

Matters to be stated in prospectus (Sec.26)— (1) Every prospectus issued by or on behalf of a public company either with reference to its formation or subsequently, or by or on behalf of any person who is or has been engaged or interested in the formation of a public company, shall be dated and signed and shall:

state such information and set out such reports on financial information as may be specified by the Securities and Exchange Board in consultation with the Central Government:

Provided that until the Securities and Exchange Board specifies the information and reports on financial information under this sub-section, the regulations made by the Securities and Exchange Board under the Securities and Exchange Board of India Act, 1992 (15 of 1992), in respect of such financial information or reports on financial information shall apply.

(a) – (d) [xxx]

(2) Nothing in sub-section (1) shall apply:

(a) to the issue to existing members or debenture-holders of a company, of a prospectus or form of application relating to shares in or debentures of the company, whether an applicant has a right to renounce the shares or not under

sub-clause (*ii*) of clause (*a*) of sub-section (*1*) of section 62 in favour of any other person; or

(b) to the issue of a prospectus or form of application relating to shares or debentures which are, or are to be, in all respects uniform with shares or debentures previously issued and for the time being dealt in or quoted on a recognised stock exchange.

(3) Subject to sub-section (*2*), the provisions of sub-section (*1*) shall apply to a prospectus or a form of application, whether issued on or with reference to the formation of a company or subsequently.

Explanation: The date indicated in the prospectus shall be deemed to be the date of its publication.

(4) No prospectus shall be issued by or on behalf of a company or in relation to an intended company unless on or before the date of its publication, there has been delivered to the Registrar for filing, a copy thereof signed by every person who is named therein as a director or proposed director of the company or by his duly authorised attorney.

(5) A prospectus issued under sub-section (*1*) shall not include a statement purporting to be made by an expert unless the expert is a person who is not, and has not been, engaged or interested in the formation or promotion or management, of the company and has given his written consent to the issue of the prospectus and has not withdrawn such consent before the delivery of a copy of the prospectus to the Registrar for

filing and a statement to that effect shall be included in the prospectus.

(6) Every prospectus issued under sub-sec. (1) shall, on the face of it:

(a) state that a copy has been delivered for filing to the Registrar as required under sub-section (4); and

(b) specify any documents required by this section to be attached to the copy so delivered or refer to statements included in the prospectus which specify these documents.

(7) [xxx]

(8) No prospectus shall be valid if it is issued more than ninety days after the date on which a copy thereof is delivered to the Registrar under sub-section (*4*).

(9) If a prospectus is issued in contravention of the provisions of this section, the company shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees and every person who is knowingly a party to the issue of such prospectus shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees, or with both.

Prospectus is a very important document, which invites/ attracts the public to invest in the company. So, it must be drafted very carefully in strict adherence to the provisions of the Companies Act, 2013. A copy of prospectus along with requisite documents has to be submitted to the Registrar of Companies for its registration. It must be issued within 90 days from the date of incorporation by an advertisement of newspaper or otherwise.

According to Section 26 of the Companies Act, 2013, a prospectus shall contain the following information.

i) Name and Address:- It shall contain the names and addresses of its Registered Office, Company Secretary (C.S), chief Finance Officer (C.F.O), Auditors, Legal Advisers, Bankers, Trustees, if any, names addresses, descriptions of the directors. The qualification shares, if any, held by the directors and the terms of their appointment, remuneration and compensation for loss of office etc.

ii) Dates:- Dates of the opening and closing of the issue and declaration about the issue of allotment letters and refunds within the prescribed time.

iii) Board of Directors, Statement:- A statement by the Board of Directors about the separate Bank Account where all monies received out of the issue are to be transferred and disclosure of details of all monies including utilized and unutilized monies out of the previous issue in the prescribed manner.

iv) Capital Structure:- It contains authorized, issued, subscribed, called up and paid up capital. Division capital

into different kinds of shares and debentures, face value of each share/debenture, whether issued at premium/discount and payable at per or in part payments i.e. along with application, at the time of allotment, first call, second call, final call etc.

v) Consent:- Consent of the Directors, auditors, bankers to the issue, expert's opinion, if any.

vi) Under writing of Issue:- Details about underwriting of issue (issued capital) names, addresses of under writers, their obligations and amount and rate of underwriting commission etc.

vii) Time Schedule:- Procedure and time schedule for allotment and issue of securities.

viii) Objects of Public Offer:- Main object of public offer, terms of present issue and such other particulars which may be prescribed.

ix) Present Business of the Company:- Main objects and present business of the company and its location, schedule of implementation of the object.

x) Preliminary Expenses:- Particulars relating to Preliminary Contracts and other preliminary expenses for promotion/incorporation of the company to be furnished.

xi) Other particulars:- Relating to risk factors specific to the project, gestation period of the project of the project, extent of progress made in the project, deadlines for completion of the project and any legal litigation or legal action pending.

xii) **Subscription Amount:-** Minimum subscription amount payable by way of premium issue of shares, otherwise than on cash.

xiii) **Details about Directors' Appointment, Remuneration and their Interest:-** Details of Directors including their appointments and remuneration and such particulars of the nature and extent of their interests in the company.

xiv) **Auditors' Report:-** A report by the auditors of the company relating to profits and losses and assets and liabilities of the company for each of the five financial years before the issue of the prospectus. The report must refer to the rates of dividends, if any, paid by the company in respect of each class of shares for each of the said years. The report of the auditors must also state separately the profits and losses of the Company's subsidiaries and also combined profits and losses.

xv) **Profits and Losses:-** Reports relating to profits and losses for each of the five financial years immediately preceding the financial year of the issue of prospectus including such reports of its subsidiaries.

In case of the company where period of five years has not elapsed from the date of its incorporation, the reports of each financial year shall be set out in the prospectus.

xvi) **Declaration about Compliance of Statutory Provisions (Sec.26(1)(c)):-** It is mandatory for the company to make declaration regarding compliance of statutory provisions such as the provisions of the Companies Act, 2013, the Securities Contracts (Regulation) Act, 1956 and the Securities and Exchange Board of India, 1952 and the rules and regulations made there under.

6. When Prospectus need not be issued

The issue of prospectus under Section 26 of the Companies Act, 2013 is not necessary in the following circumstances even though the shares are offered and application forms issued to public by the company:

1. Where a person is a *bona fide* invites to enter into an underwriting agreement with regard to shares or debentures.

2. Where shares or debentures are not offered to the public.

3. Where the shares or debentures offered are in all respects uniform with shares or debentures already issued and quoted at a recognized Stock Exchange.

4. Where the shares or debentures are offered to the existing holders of shares or debentures respectively.

5. Where a prospectus is published as a newspaper advertisement, it is not necessary to specify the contents of the memorandum, or the names etc. of the signatories to the memorandum or the number of shares subscribed for by them.

7. Deemed Prospectus (Sec.25)

Where a company allots or agrees to allot any securities of the company with a view to all or any of those securities being offered for sale to the public, any document by which offer for sale to the public is made, shall for all purposes be deemed to be a prospectus issued by the company.

It is to be noted that 'deemed prospectus' would carry the same effect as to prospectus in respect of liability, in respect of mis-statement. A 'deemed prospectus' has an evidentiary value according to Section 24(2) of the Act, 2013.

8. Shelf Prospectus (Sec.31)

In this context expression 'shelf prospectus' means a prospectus in respect of which securities or classes of securities included therein are issued for subscription in one or more issues over a certain period without the issue of a further prospectus.

At the stage of first offer of securities shelf prospectus has to be filed with the Registrar of Companies which shall indicate the period not exceeding one year as the period of validity of such prospectus, which shall commence from the date of opening of the first offer of securities without prospectus.

Thus, no further prospectus is required in case of second or subsequent offer of securities during the validity period of such prospectus, that is to say 'shelf prospectus'.

9. Red Herring Prospectus – Prior to issue of Prospectus (Sec.32)

In this context expression 'Red Herring Prospectus' means a prospectus which does not include complete particulars of the quantum or price of the securities included therein.

In terms of Section 32(1) a company proposing to make an offer of securities may issue a red herring prospectus prior

to the issue of prospectus. Thus, a red herring prospectus has to be filed with the Registrar of Companies at least three days prior to the opening of the subscription list and the public offer as provided under Section 32(1) of the Companies Act, 2013.

10. Misstatement of Prospectus (The Golden Rule)

The term 'misstatement' has not been defined by Companies Act, 2013. However, from Section 34 of the Act, 2013, misstatement is a statement which is untrue or misleading in form or context in which it is included or where any inclusion or omission of any matter is likely to mislead.

Prospectus is a key to open the financial position of a company. It is a window, through which an investor can look into the soundness of a company's venture. Basing/inspiring on the information furnished in the prospectus, investors would come forward to invest. Therefore, prospectus must disclose truth, whole truth and nothing but truth. There must be full, frank and honest disclosure of all material facts. There must not be concealment of material facts. A prospectus containing false misleading ambiguous or fraudulent statements of material facts or suppressing facts is termed as 'misleading prospectus' containing false information/ misstatements/untrue statement may be published to attract the investors.

An untrue statement or an omission to furnish a material fact amounts to suppression of material fact or misrepresentation is a serious mistake/blunder/wrong as it misleads the investors. The aggrieved investor can approach court for appropriate remedy and the company and officials concerned, who are instrumental/

responsible for publication of such false prospectus, will have to face civil and criminal liability.

There are two kinds of untrue/mis-statements, namely —

a) Omission to state a material fact, which is calculated to mislead the investors, and

b) The inclusion of a statement, which is misleading in the form and the context in which it is included.

Remedies: An aggrieved investor as a consequence of a mis-statement of a prospectus is entitled to the following remedies –

i) Recision of Contract:- An aggrieved can rescind/cancel/ repudiate the contract and claim return/refund of his money/ investment.

ii) Damages for deceit:- The term 'deceit' is a tortuous act (civil wrong), which connotes fraud. The aggrieved is subjected to deceit as a consequence of mis-statement of prospectus and is entitled to claim damages/compensation.

iii) Statutory Compensation (Sec.35):- According to Section 35 of the Companies Act, 2013 if a prospectus, which invites persons to subscribe for shares or debentures contains untrue statements so as to cause damage to those who have subscribed on the faith of those statements, every Director, promoter or persons authorizing the issue of the prospectus is liable to pay compensation.

Liability for untrue statements in prospectus: Prospectus must always disclose truth, only/whole truth and nothing but truth. If there is any concealment or suppression of any material fact, it amounts to 'Misleading Prospectus'. If a prospectus contains any misstatement or concealment of any material facts or circumstances which may improperly influence and mislead the mind of the reader so as to deceive him into becoming an allottee of shares. [*Peck v. Gurney* (1873) LR 6 HL 377].

Mis-statement imposes civil and criminal liability under Section 35 and 34 of the Companies Act, 2013 respectively on the following persons.

i) Every person who is a director of the company at the time of the issue of the prospectus.

ii) Every person who has authorized himself to be named and is named in the prospectus as a director.

iii) Every person who has authorized himself to be named as future directors.

iv) The promoter of the company.

v) Every person who has authorized the issue of the prospectus.

vi) Experts i.e. an engineer, a valuer, an accountant and any other person whose profession gives authority to a statement made by him.

Golden Rule or Golden Legacy as to framing of prospectus: The person authorised to issue prospectus must take reasonable care that there is no misrepresentation or concealment of any material fact. Otherwise, the contract is voidable at the option of the allottee. This rule is popularly known as 'Golden Rule'. It is laid down by Vice Chancellor Kindersley in –

***New Brunswick and Canada Rly. Co. v. Muggeridge* (1860) 1 Dr. and Sm. 363:** In the following words –

'Those who issue prospectus holding out to the public the great advantages which will accure to persons who will take shares in a proposed undertaking, and inviting them to take shares on the faith of the representations therein contained, are bound to state everything with strict and scrupulous accuracy and not only to abstain from stating as fact that which is not so, but to omit no one fact within their knowledge, the existence of which might in any degree affect the nature or extent and quality of the privileges and advantages which the prospectus holds as inducement to take shares'.

Prospectus must be read as a whole and taking whole thing together. It should not give false impression.

In **R.V. Kylsant** – In the instant case, the statements in the prospectus were literally true, but materially false. The statement that dividend paid was true. But it was paid not out of trade profit,

but out of secret reserves. It was held to be false and the Managing Director was held guilty of fraud.

The persons concerned for misstatement of prospectus are liable for civil and criminal liability, if there is any material fact or wanting in any material fact.

Civil Liability (Sec.35): Section 35 of the Companies Act, 2013, imposes civil liability. The persons responsible for misstatement/untrue statements of prospectus are liable to pay compensation to the persons, who subscribed shares and debentures relying on such false information in the prospectus. Such persons include directors, promoters, experts etc.

The section provides that the directors, promoters and every other person who is authorized to issue the prospectus of a company shall be liable to pay compensation to the investor for any loss sustained by him due to untrue statement in the prospectus. The liability of the directors or promoters, as the case may be, is joint and several and they may recover contribution from others who are guilty of misrepresentation (Section 35(1).

A statement is deemed to be untrue if it is false in form and context in which it is included. This is well illustrated by the case in–

Greenwood v. Leather Shod Wheel Co. (1900) 1 Ch. 421 – in this case, a wheel manufacturing company issued a prospectus in which it was stated that orders had already been received from House of Commons to supply wheels for the trolleys in use in the House. In fact, not a single order was obtained except for trial and by way of experiment. The Court held that the prospectus contained untrue statement and the directors were held liable.

Defences (Sec.35(2): The persons (viz. director, expert etc.) subject to civil liability may plead/invoke immunity/exemption from liability as stated below:

Defences to civil liability available to a director [Sec.35(2)]: In an action for compensation under Sec.35(1) the director concerned can plead the following defenses, as stated in Sec.35(2):

i) *Withdrawal of consent*: A director may withdrew his consent to be a director, before the prospectus was issued and that the prospectus was issued without his authority or consent.

ii) *Without knowledge*: A director may plead that the prospectus was issued without his knowledge or consent, and that on becoming aware of its issue, he forthwith gave reasonable public notice of the fact that it was issued without his knowledge or consent.

iii) *Ignorance of untrue statement*: A director might be ignorant of untrue statements made in the prospectus. As soon as he became aware of any untrue statement in the prospectus, he may withdrew his consent to the prospectus and gave reasonable public notice of the withdrawal and of the reason therefor. It has also to be proved that such public notice was given before the allotment of shares.

iv) *Reasonable ground for belief*: A director can invoke/seek immunity from liability with regard to statements made by an expert, that the person making the statement was competent to make it, and as regards the statements by other persons that he had reasonable ground to believe, and did up to the allotment of shares or debenture believe that the statement was true.

In *Adams v. Thrift* (1915) 2 Ch. 21) – the director on being sued by the plaintiff for compensation in respect of a false statement in the prospectus, pleaded that he had enquired about the perfectness of the issue from the promoters who had affirmed that everything was in order. The director was nevertheless held liable as the promoter's version was not held to be a reasonable ground for belief for the director. He ought to have obtained a report of competent people as to the material facts in the said prospectus.

v) *Reliance on expert's opinion*: The director shall also be protected if he proves that as regards the untrue statement purporting to be made by an expert; it was a correct and fair representation of the statement, therefore he had reasonable ground to believe that the said expert was competent and that

the expert had complied with the provisions of Section 26 of the Act, 2013.

vi) *Statement based on public official document*: The director shall not be liable if he proves that as regards every untrue statement purporting to be a statement made by an official person or from public official document, it was correct and fair extract from the document.

It may be stated that the earlier Companies Act, 1956 made no distinction between innocent mis-statement and fraudulent mis-statement in the matter of civil liability for mis-statements in prospectus under Section 62 of that Act, but the Companies Act, 2013 does recognize such distinction under Section 35 which relates to civil liability for mis-statement.

Similarly, there was no provision for class action under the preceding Companies Act, 1956, but this has been recognized under Section 37 of the Companies Act, 2013, which provides that a suit may be filed or taken under Section 34 or 36 of the Act of 2013 by any person, group of persons or any association of persons affected by any mis-leading statement or the inclusion or omission of any matter in the prospectus with intent to defraud.

Defences to civil liability available to an expert [Sec.35(2)]: According to Sec.35(2) the following defences shall be available to an expert in an action for compensation.

i) That having given his consent under Section 58 to the issue of the prospectus, he withdrew it in writing before delivery of a copy of the prospectus for registration.

ii) That after filing a copy of the prospectus with the Registrar and before allotment there under, he, on becoming aware of the untrue statement, withdrew his consent in writing and gave reasonable public notice of the withdrawal and of the reason there for, or

iii) That he was competent to make the statement and that he has reasonable ground to believe, and did up to the time of the allotment of the shares or debentures, believe, that the statement was true.

Right of Directors and Experts to claim Indemnity [Sec.35(2)]: According to Section 35(2) the directors and experts can claim indemnity from every other person was authorised the issue of the prospectus, where –

a) The prospectus specifies the name of a person as a director, or as having agreed to become a director, and he has not consented to become a director, or has withdrawn his consent before the issue of the prospectus, and has not authorisedor consent to the issue thereof (Section 35(2)(a)).

b) The consent of a person is required as an expert under Section 58 to the issue of the prospectus, and he either has not given the consent or has withdrawn it before the issue of the prospectus (Section 35(2)(b)).

Right to recover contribution [Sec.35(3)]: According to Section 35(3) any person who becomes liable to pay compensation under Section 35 may recover contribution, as in case of contract, from any other person who if sued separately, would have been liable to make the same payment, unless the former person was, and the latter person was not, guilty of fraudulent misrepresentation.

Compensation under Section 75, Indian Contract Act: It has been already noted that when the consent of a person has been obtained by fraud or misrepresentation, he has a right to avoid the contract under Section 19 of the Indian Contract Act. Apart from that, according to Section 75 of that Act, a person who rightfully rescinds a contract is entitled to compensation for any damage which he has sustained through the non-fulfillment of the contract.

Compensation under (English) Misrepresentation Act, 1967: In England the Misrepresentation Act, 1967 allows compensation to be claimed even in respect of non-fraudulent statements, if a person has suffered any loss due to such mis-statement. Apart from that the Act also permits award of damages in lieu of rescission of contract, in case of non-fraudulent misrepresentations.

Criminal Liability (Section 34):

i. Liability for non-disclosures (Sec.26): It has been already noted above that according to Section 26 every prospectus shall state matters specified under the Companies Act, 2013 viz. information regarding the objects of the company, shares, managerial personnel, minimum subscription, preliminary expenses, and working capital etc. has to be given. According to the amended provisions of Section 56 in 1988, every application form for subscription to the shares or debentures is also to be accompanied by 'a memorandum containing salient features of a prospectus.' If the above stated disclosures are not made the person responsible for the same shall be punishable with fine which may extend to Rs.5000/- A person may avoid his liability for non-disclosures by proving:

a) That he had no knowledge of the matter not disclosed.

b) That the non-compliance or contravention of the above requirement arose on account of honest mistake of fact on his part; or

c) If, in the opinion of the Court, the non-disclosures were immaterial, or having regard to all the circumstances of the case, the person sued ought to be excused.

ii. Liability for Mis-statements (Sec.34): Section 34 recognizes criminal liability of every person who authorised the issue of the prospectus in respect of untrue statements contained in the prospectus. Section 34 says that where prospectus includes any untrue statement, every person who has authorized the issue of the prospectus shall be punishable under Section 447 of the Act, which provides punishment for fraud. Any person found guilty of fraud may be punished with:

i) Imprisonment for a term which may not be less than six months but which may extend to ten years, and

ii) Fine which shall not be less than the amount involved in the fraud, but which may extend to three times the amount involved in the fraud, or

iii) Both imprisonment and fine (Section 447 of Companies Act, 2013).

However, he shall not be criminally liable if he proves that the statement was immaterial or that he had a reasonable ground to believe that it was true.

An expert who has given the consent as required by Section 26, shall not be criminally liable for the purpose of Section 35(1).

11. Underwriting Commission and Brokerage

Underwriting Commission: A public company which invites the public to subscribe for its shares or debentures must ensure that the issue is subscribed by the public. As such, it is willing to pay anyone a certain commission on all shares or debentures offered to the public, if he guarantees that if any of these are not taken up by the public, he will take them up. The commission, so paid, is known as 'underwriting commission'. Even if the company is sure that all the shares or debentures will be taken up by the public, it is advisable for it to get the shares or debentures underwritten to avoid the risk arising from certain unforeseen contingencies which may endanger the success of the issue.

An underwriter, therefore, is a person or a body corporate such as a Bank or a financing institution who agrees to take specified number of shares or debentures in the event of the public not subscribing for them in consideration of a commission which is called 'underwriting commission'. The company may also make an agreement with financial institutions who, in consideration of the commission, agree to subscribe for the shares or debentures to the extent to which they are not taken up by the public.

An underwriter's agreement is 'an agreement whereby, previously to an offer of a company's shares to the public for subscription, some person undertakes, in consideration of a commission to take the whole or a portion of such (if any) of the offered shares as may not be subscribed for by the public'.

The underwriting commission may be paid subject to the following conditions:

i) The payment of commission must be authorized by the articles.

ii) The rate of commission should not exceed five per cent of the price at which the shares are issued. In case of debentures it should not exceed 2.5 per cent.

iii) The rate of underwriting commission must be stated in the prospectus or statement in lieu of prospectus.

iv) The prospectus must also specify the number of shares or debentures which have been underwritten.

v) A copy of the underwriting contract should be filed with the Registrar of Companies.

Thus, the underwriters are persons, who charge a commission in return of their agreeing to buy shares in case they are not taken up by the public within a specified time.

Brokerage: Brokerage is different from underwriting commission. A broker is a kind of professional middle man who brings about a bargain between a vendor and as purchaser for which he is paid certain brokerage. They induce customers to subscribe for, and thus assist the company in selling its shares or debentures. Brokerage may be understood as a payment made by a company to a broker who agrees to place its shares or who finds out some person to take its shares. Thus a broker is employed by company for placing its shares or finding out certain persons who may take shares and for this service the broker is paid commission which is known as brokerage. Thus brokerage is the payment to 'stock brokers, bankers and the like, who exhibit prospectuses and send them to their customers and by mediation the customers are induced to subscribe.'

12. Allotment of securities by company (Section 39)

Sections 39 of Part-III of the Companies Act, 2013 lays down the provisions relating to Section 39 of the Companies Act, 2013 lays down the provisions relating to 'Allotment of Securities by Company'. It reads as follows –

(1) No allotment of any securities of a company offered to the public for subscription shall be made unless the amount stated in the prospectus as the minimum amount has been subscribed and the sums payable on application for the amount so stated have been paid to and received by the company by cheque or other instrument.

(2) The amount payable on application on every security shall not be less than five per cent. of the nominal amount of the security or such other percentage or amount, as may be specified by the Securities and Exchange Board by making regulations in this behalf.

(3) If the stated minimum amount has not been subscribed and the sum payable on application is not received within a period of thirty days from the date of issue of the prospectus, or such other period as may be specified by the Securities and Exchange Board, the amount received under sub-section (1) shall be returned within such time and manner as may be prescribed.

(4) Whenever a company having a share capital makes any allotment of securities, it shall file with the Registrar a return of allotment in such manner as may be prescribed.

(5) In case of any default under sub-section (3) or sub-section (4), the company and its officer who is in default shall be liable to a penalty, for each default, of one thousand rupees for each day during which such default continues or one lakh rupees, whichever is less.

Application and Allotment of Shares: An application for shares is an offer by a prospective shareholder of a company to take shares. 'Allotment' is the acceptance by the company of that offer. Allotment results in a binding contract between the company and the applicant.

The term 'allotment' is not defined in the Act, Broadly speaking, allotment is the appropriation to an applicant by a resolution of the directors of a company of a certain number of shares in the company in response to an application (Spitzel vs. Chinese Corpn. (1899) 80 LT 347).

In ***Sri Gopal Jalan& Co. v. Calcutta Stock Exchange Assn. Ltd.*** **(1963) 33 Comp. Cas. 802,** the Supreme Court

explained allotment of shares as 'the appropriation out of the previously unappropriated capital of the company, of a certain number of shares to a person. Till such allotment the shares do not exist. It is on allotment that shares come into existence.'

Sterling, J. in Spitzol v. Chinese Corporation **(1889) 80 LT 351,** says that an allotment of shares is an appropriation by the directors or the managing body of the company of shares to a particular person.

Allotment of shares carries a special significance in the Company Law. The persons desirous of purchasing 'shares' of the company apply for the same in the prescribed form. This is technically called 'proposal to purchase'. The said proposal when accepted, the company issues acceptance which is called 'allotment'. In '***Gopal Jalan v. Calcutta Stock Exchange Association,*** reported in (1963) 1 Comp. LJ 198, allotment has been described as 'allotment means the appropriation out of previously unappropriated capital, of a certain number of shares to a person'. Thus allotment implies direct issue of shares by a company. Till such time, a company does not allot shares, the person cannot become shareholder. For this purpose, as discussed earlier, the company has to issue prospectus, which inter alia contains terms and conditions of allotment.

Allotment of Shares/Securities (Sec.39): Issue and distribution of application forms for shares and other securities is an invitation for invest (or an invitation to offer). Submission of applications by applicants/public to purchase shares in response to the invitation is an 'offer'. When the company accepts the application to issue shares is an 'allotment'. An allotment to be valid,

1. No allotment unless minimum subscription received (Sec.39): When the shares of a company are offered to the public for subscription the prospectus is to specify the amount of minimum subscription, i.e. the amount which, in the opinion of the Board of Directors, must be raised by the issue of share capital in order to provide for the purchase price of the property purchased or to be purchased, preliminary expenses payable by the company, and working capital. No allotment of shares can be made unless the

amount mentioned in the prospectus as the minimum subscription has been received.

2. Application money (Sec. 39(2)): The amount payable on application of each share shall not be less than 5% of the nominal amount of each share.

3. Application money to be kept in a bank: All moneys received from applicants for shares shall be deposited and kept deposited in a Schedule Bank –

a) until the entire amount payable on applications for shares in respect of the minimum subscription has been received by the company.

4. Repayment if minimum subscription not received: If the minimum subscription is not received within 30 days after the first issue of the prospectus, all moneys received from applications for shares shall be forthwith repaid to them without interest within 15 days from the expiry of 30th day. In case any such money is not so repaid,the directors of the company shall be jointly and severally liable to repay that money with interest @ 6% per annum from the expiry of 15th day due for payment. However, a director may not be liable if he proves that the default in the repayment of the money was not due to any misconduct or negligence on his part.

5. Effect of irregular allotment: An allotment which is made in contravention of the above provisions viz. an allotment without receiving the required application money, or without obtaining minimum subscription, shall be voidable at the instance of the applicant within two months of the allotment, Such allotment shall be voidable even if the company is in the course of being wound up. If any director knowingly permits irregular allotment as mentioned above, he shall be liable to compensate the company and the allottee respectively for any loss, damages or costs which the company or the allottee may have sustained or incurred thereby.

6. No opening of subscription list before 5th day after the issue of prospectus: No opening of the subscription list can be there, i.e. no allotment of shares or debentures can be made,

until the beginning of the 5th day after the issue of the prospectus, or such later time, if any, as may be specified in the prospectus.

7. Listing with the stock exchange (Sec.40): Listing of all public issues with the stock exchange has been made compulsory. According to Section 40 every company intending to offer shares or debentures to the public for subscription by the issue of a prospectus shall, before such issue, make an application to one or more recognized stock exchanges for permission for the shares or debentures intending to be so offered to be dealt within the stock exchange or each such stock exchange. The prospectus should state the name(s) of the stock exchange or the stock exchange to whom application for the aforesaid permission has been made. If the permission sought has not been granted by the stock exchange or each such stock exchange, any allotment made in pursuance of the prospectus shall be void.

8. Return as to allotments: Whenever a company having share capital makes an allotment of its shares, the company shall, within 30 days thereafter file with the Registrar the Return of the allotment, i.e. the company should submit a statement indicating the number and nominal amount of the shares allotted, the names, addresses, and occupations of the allottees, and the amount, if any paid or due and payable on each share including the copies of the documents authorizing the issue of such shares, have also to be filed with the Registrar, within 30 days after the allotment.

If there is default to file the Return, every officer of the company who is in default shall be liable for punishment under the Act.

13. Prospectus of Foreign Companies (Section 387)

No person shall issue, circulate or distribute in India any prospectus offering to subscribe for securities (shares etc.) of a company incorporated or to be incorporated outside India, whether the company has or has not established, or when formed will or will not established, a place of business in India, unless the prospectus is dated and signed and contains particulars with respect to following matters:

i) Documents or instruments relating to the formation of the company.

ii) Rules by which incorporation of the company was effected.

iii) The name of the place in India where above documents of the foreign company can be inspected and copies thereof in the English language.

iv) The place, date and country where company has been incorporated.

v) In case the company has established its business in India, the Principal offices of the company in India with full address thereof.

Lecture-VII
SHARES

This lecture covers —

1. Share: Meaning, Definition and Nature.
2. Kinds of Shares.
3. Transfer of Shares.
4. Transmission of Shares.
5. Share Certificate and Share Warrant.
6. Lien on Shares.
7. Surrender and Forfeiture of Shares, and
8. Bonus Shares.

1. Share: Meaning, Definition and Nature

The expression 'share' in the literal sense means, 'a part' or 'a division' or 'a portion'. In Company Law, it refers to unit of the capital of a public limited company. A person who owns share/ shares is called 'shareholder'. In other words, the capital of a public limited company is divided into small units called 'shares'. A share is an interest of a shareholder in a company. A private company can start business after registration/ incorporation. But a public limited company cannot start business until and unless the certificate of commencement of business is issued. For this purpose a public limited company has to issue prospectus within 90 days of its incorporation and should secure minimum subscription within 30 days. Therefore, share and share capital forms basis for creation and existence of a public limited company. The rights and liabilities of a shareholder are regulated by the articles of association of the company.

The word 'share' ordinarily means a part or definite portion of a thing owned by a number of persons in common. It contemplates something owned in common by two or more persons and has

reference to that part of the undivided interest which belongs to some of them.

In *Peter's American Delicacy Co. Ltd. v. Health* (1939) 61 CLR 457) – Dixon J says, 'primarily a share in a company is a piece of property conferring right in relation to distribution of income and capital'.

A share is not a sum of money, but represents an interest measured by a sum of money and make up of diverse rights contained in the contract evidenced by the articles of association of company.

Definition: It is very difficult to define 'share'. Many authors defined it in different/ various ways as follows:

According to **Dixon, J.** 'Primarily a share in a company is a piece of property conferring right in relation to distribution of income and capital'. [*Peter's American Delicacy Co. Ltd. v. Heath*, (1939) 61 CLR 457].

'A share is a right to a specific amount of the share capital of a company carrying with it certain rights and liabilities while the company is a going concern and on its winding up'. [*ChiranjitlalChowdary v. Union of India*, (1950) SCR 869].

According to Section 2(46) of the Companies Act, 1956, 'share' means share in the share capital of a company, and includes stock except where a distinction between stock and shares is expressed or implied.

According to Section 2(84) of the Companies Act, 2013, 'share' means a share in the share capital of a company and includes stock.

The best definition given by *Farewell JinBarland's Trustee v. Steel Brothers* (1901) 1 Ch. 279) defined 'share' as the interest of a shareholder in the company measured by a sum of money for the purpose of liability, in the first place, and of dividend in the second, but also consisting of a series of mutual covenants entered into by all the shareholders *inter se* in accordance with the Companies Act.

The Supreme Court of India approved the above definition of share in Commissioner of Income Tax v. Standard Vacuum Oil Company (1966) 1 Comp. LJ 187 (SC), and observed, 'by a share in a company is meant not any sum of money but an interest measured by a sum of money and made up of diverse rights conferred on its holders by the articles of the company which constitute a contract between him and the company'.

Thus, it may be concluded that a share is a right to participate in the profits made by a company while it is a going on concern and declares dividends and in the assets of the company in the event of its being wound up (*Bacha F. Guzder v. Commissioner of Income Tax* (AIR 1955 SC 75).

Nature of Share: As regards nature of share, it is not a sum of money but carries with it a bundle of rights and liabilities. It may therefore, be called as an interest measured by a sum of money.

Shares form basis for capital of a public limited company. Share is an interest of a shareholder. It fixes the rights and obligations of the shareholder. It is a movable property since the shares are easily transferable from one person to another in an open market.

A share entitles the holder to receive a proportionate part of the profits of the company; to take part in the management of the company's business in accordance with the Articles; to receive a proportion of the assets in the event of winding up and all other benefits of membership. A share also carries some liabilities i.e. the liability to pay the full value in winding up.

According to **Lord M.R.Greene**, a man's movable property is of two kinds, viz. choose-in-possession and choose-in-action. Choose in possession means property, which you have in your control and in your actual physical possession but choose-in-action means property of which you do not have immediate possession but you have a right to it, which can be enforced by a legal action. This right is generally evidenced by a document, for example, a railway receipt. A share in a company is also a choose-in- action and the share certificate is the evidence of it.

Section 138 of the Companies Act, 2013 provides that a share or other interest of any member in a Company is a movable property transferable in the manner provided by the articles of the company but it is not a negotiable instrument.

Section 139 further provides that each share in a company shall be distinguished by its appropriate number, provided that nothing in this section shall apply to the shares held by a depository.

In India, a share has been regards as 'goods' within the meaning of Section 2(7) of the Sale Goods Act, 1930 which says 'Goods means any kind of movable property other than actionable claims and money, and includes stock and shares.'

But it is to be remembered that shares are not ordinary but a peculiar kind of movable property and they cannot pass from one hand to another like ordinary goods. [*Vadilal Sarabhai v. ManikjiPestonjiBharucha*, AIR 1923 Bom. 423].

Hence shares in a company in India are goods and not mere choose-in-action. It was so held in the case of *Hazari Mull Sohan Lal v. Satish Chandra Ghose*, (1888) 46 Cal. 9 LR 331.

Features of Share:

i. Share is a definite part of the authorised share capital of a company.

ii. Share is a movable property transferable in the manner provided by the articles.

iii. It is serially numbered so that the shares held by each member may be easily identified.

iv. It carries with it the rights and obligations of the shareholder which remains shares of the company during its subsistence; and

v. It is, in fact, that interest of the shareholder on the basis of which the shareholder does not have right over the assets of the company; he merely acquires right to share in the profits of the company and bear its losses to the extent indicated thereon.

Share and Stock: As stated above, the capital of a public limited company is divided into small units called 'shares'. The shareholder may be required to subscribe (to pay) in full the total face value of the share or by way of installments viz. application, allotment, first call, second call, final call etc. Thus, a share may be fully paid up or partly paid up. The term 'stock' or 'joint stock' is nothing but an alternate name for shares.

As contained in Section 2(84) of the Companies Act, 2013 the term 'share' includes stock except whether a distinction between stock and share is expressly or impliedly made.

Lord Hatherley in *Morris v. Aylmer* (1875) LR 7 HL 717 (725), *inter alia* observed that stock is 'simply a set of shares put together in a bundle'. Stock is created by the conversion of fully paid shares into stock provided such conversion is authorized by the articles of the company (Section 61(1)(c) of Companies Act, 2013). The main advantage of converting shares into stock is that it greatly facilitates the maintenance of register and issue of certificates. Stock, unlike shares, may be sub-divided into fractions. The voting rights and dividend of stock holders are governed by Regulations framed under the Companies Act, 2013. The main difference between shares and stock is noted below:

Share	Stock
1. Share may be fully paid up or partly paid up (non-paid or unpaid).	1. Stock originates from fully paid up shares.
2. A share cannot be broken up in to parts. In other words, share is not divisible.	2. Stock unless the articles provide otherwise may be broken up in to any division. In other words, stock is divisible.
3. Share has a nominal value.	3. Stock has no such nominal value.
4. Any new company can float shares for subscription.	4. Only fully paid up shares can be converted into stocks and then floated.

5. Only fully paid up shares can be converted in to stock.	5. Stock can be reconverted in to shares under Sec.61 of the Companies Act.
6. Shares can be issued to public directly.	6. Stock cannot be issued directly to public.

Conversion of shares in to stock: A company limited by shares may, if authorized by its Articles, by a resolution passed in a general meeting, convert into fully paid-up shares into stock. Articles 35 to 38 of Table F of Schedule I of the Companies Act, 2013 provides that:

Article 35 – The Company may, from time to time, by ordinary resolution increase the share capital by such sum, to be divided into shares of such amount, as may be specified in the resolution.

Article 36 – Subject to the provisions of Section 61, the company may, by ordinary resolution –

a) Consolidate and divide all or any of its share capital into shares of larger amount than its existing shares.

b) Convert all or any of its fully paid-up shares into stock, and reconvert the stock into fully paid-up shares of any denomination.

c) Sub-divide its existing shares or any of them into shares of smaller amount than is fixed by the memorandum.

d) Cancel any shares which, at the date of the passing of the resolution, have not been taken or agreed to be taken by any person.

Article 37 – Where shares are converted into stock –

a) The holders of stock may transfer the same or any part thereof in the same manner as, and subject to the same regulations under which, the shares from which the stock arose might before the conversion have been transferred or as near thereto as circumstances admit:

Provided that the Board may, from time to time, fix the minimum amount of stock transferable, so however, that such minimum

shall not exceed the nominal amount of the shares from which the stock arose.

b) The holders of stock shall, according to the amount of stock held by them, have the same rights, privileges and advantages as regards dividends, voting at meetings of the company, and other matters, as if they held the shares from which the stock arose; but no such privilege or advantage (except participation in the dividends and profits of the company and in the assets on winding up) shall be conferred by an amount of stock which would not, if existing in shares, have conferred that privilege or advantage.

c) Such of the regulations of the company as are applicable to paid-up shares shall apply to stock and the words 'share' and 'share-holder' in those regulations shall include 'stock' and 'stock-holder' respectively.

Article 38 – The Company may, by special resolution, reduce in any manner and with, and subject to, any incident authorized and consent required by law –

a) Its share capital.

b) Any capital redemption reserve account, or

c) Any share premium account.

2. Kinds of Shares

Before Companies Act, 1956, a public limited company could issue four kinds of shares, namely:

1. Preference Shares.
2. Ordinary/Equity Shares.
3. Deferred Shares; and
4. Bonus Shares.

Under Section 86 of the Companies Act, 1956 and the Companies Act, 2013, a public company can issue two kinds of shares, namely –

1. Preference Shares (Section 43). (Section 85(1) of the Companies Act, 1956 and Section 43 of the Companies Act, 2013), and
2. Equity Shares (Section 43). (Section 85(2) of the Companies Act, 1956 and Section 43 of the Companies Act, 2013).

1. Preference Shares [(Sec.85(1)]: Preference shareholders are given priority over equity shareholders not only at the time of payment of dividends but also at the time of repayment of share capital in the event of winding up. Thus, Sec.85 of the Act, confers on preference shareholders two rights, namely:

i. Preferential right to claim dividend; and

ii. Preferential right for claiming repayment of capital.

The equity share capital shall be only of two kinds, namely–

i) Equity shares with voting rights, or

ii) Equity shares with differential rights as to dividend, voting or otherwise in accordance with rules subject to such conditions as may be prescribed by the Central Government.

Sweat Equity Shares (Sec.54):- A new Section 79.A was inserted, by the Companies (Amendment) Act, 1999 provided for issue of Sweat Equity Shares by a company incorporated, formed and registered under the Companies Act and also included its subsidiary companies incorporated in a country outside India.

As provided in Explanation to the section, the term Sweat Equity Shares connote the shares issued by the company to employees or directors at a discount or for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions.

Similar provision has been incorporated in Section 54 of the Companies Act, 2013 which provides that a company may issue sweat equity shares of a class of shares already issued subject to the compliance of the following conditions –

a) The issue of such shares is authorized by a special resolution passed by the company in the general meeting.

b) The resolution specifies the number of shares, current market price, consideration, if any, and the class or classes of directors or employees to whom such equity shares are to be issued.

c) [xxx]

d) The sweat equity shares of a company whose equity shares are listed on a recognized stock exchange are issued in accordance with the regulations made by the Securities & Exchange Board of India (SEBI).

Provided that in case of a company whose equity shares are not listed on any recognized Stock Exchange, the sweat equity shares are issued in accordance with the guidelines as may be prescribed.

The rights, limitations and provisions as are for the time being applicable to equity shares shall be applicable to the sweat shares issued under Section 54 of the Act and the holders of such share shall rank *paripassu* with other equity share-holders (Section 54(2).

Kinds of Preference Shares: Preference shares may be sub-divided under the following heads, namely:

a) Cumulative Preference Shares.

b) Non-Cumulative Preference Shares.

c) Participating Preference Shares.

d) Non Participating Preference Shares.

e) Convertible Preference Shares.

f) Non-Convertible Preference Shares; and

g) Redeemable and Irredeemable Preference Shares (Sec.80).

a) Cumulative Preference Shares: It ensures dividend every year. If the Company is unable to pay dividend in any financial year on account of no profit, the arrears of such dividend is accumulated, carried forward and paid out of the profits of the subsequent years.

b) Non-Cumulative Preference Shares: The Articles of Association of the Company makes no provision for accumulation of the dividend. In this case, the dividend due (on account of no

profit) will not be accumulated and will not be carried forward for payment against subsequent years' profits.

c) Participating Preference Shares: In this case, the shareholder is entitled to certain amount of dividend calculated at a fixed rate. In addition, he claims from the surplus amount after distribution of his fixed rate of dividend along with the equity shareholders. He is also entitled to be paid the amount of capital in the event of winding up.

d) Non-Participating Preference Shares: In this case, the shareholder is entitled to the fixed rate of dividend and cannot claim from the surplus as above.

e) Convertible Preference Shares: These are the shares, which entitle their holder to convert them in to equity shares within a certain period.

f) Non-Convertible Preference Shares: These are the shares, which do not confer on their holder a right of conversion in to equity shares.

g) Redeemable Preference Shares (Sec.55): Under Section 55 of the Companies Act, 2013 a company has the power to issue preference shares. But there must be an authority in the Articles of Association to issue such shares. However, the option of redemption lies with the company. The company may choose to pay back the holders of such shares. Paying back is known as redemption.

Thus if the amount of shares is paid back then such shares are known as redeemable preference shares and if there is no provision to pay back the amount of shares before the winding-up then they are known as irredeemable preference shares.

2. Equity Shares (Sec.43): Earlier, these shares were called 'ordinary shares'. According to Sec.43 of the Companies Act, 2013, 'Equity Share Capital' means, all share capital, which is not preference share capital. Equity shareholders do not have any priority (like preference shareholders) as to the distribution of dividends. In a public limited company, majority members are equity shareholders.

Distinction between Preference and Equity Shares:

Following are the notable points of distinction between the Preference and Equity Shares.

Preference Share	Equity Share
1. The preference shareholders have no voting rights.	1. The equity shareholders have voting rights.
2. The preference shares redeemable than equity shares.	2. The equity shares are the real risk-takers, and are the real shares.
3. Generally, dividend rate or amount is pre-fixed in case of preference shares.	3. The dividend is not pre-fixed. It depends upon the availability of the profits after payment of dividends to preference shares and debentures.
4. Firstly, the dividends on preference shares shall be paid.	4. After paying the dividends to preference shares, then only the dividends on equity shares shall be decided and paid, depending upon the availability of profits.
5. The dividend rate is pre-fixed, and the income is guaranteed on them.	5. The dividend is not pre-fixed and the income is not guaranteed.
6. In case of cumulative preference shares, the prefixed dividend shall be carried to the next year, if there are no profits in the current year.	6. There is no such arrangement in equity shares. Dividends may be paid or not. If profits are made, then only the dividends are paid to equity share-holders, that too after payment of dividends to the preference shares.

3. Transfer of Shares (Section 44)

The term 'transfer' means "to convey or pass the right of one person over to another". It is an act of parties or of law, by which the title to property is conveyed from one person to another. The significant feature of a public limited company is 'transfer of shares'. The shares are considered as movable property and are transferable as provided by the articles of the company (Sec.44). In ***ThenppaChettiar v. Indian Overseas Bank Ltd.*** **(1943) 13 Comp. Cas. 202,** it was observed that 'the right of a shareholder to transfer his shares in a company is absolute as it is inherent in the ownership of the shares, but it can be restricted by contract which has to be found in the Articles of Association of the company.'

Thus, every shareholder has a right to transfer his shares in an open market without the consent of other shareholders subject to express restriction if any to that effect by articles. However, the articles of the company may empower the directors to refuse to register the transfer. In case, the directions are induced to register the transfer by concealment or fraud, such transfer is invalid and the transfer cannot avoid liability on the shares.

According to Section 44 of the Companies Act, 2013, the shares or debentures or other interests of any member in a company shall be movable property, transferable in the manner provided by the Articles of the company. Thus, every member of a public limited company has a statutory right to transfer his shares in the manner prescribed by the Articles of the company.

In *Re Bahia & San Franscisco Rly. Co.* (1868) 3 QB 584l, 595), Blackburn J has held, 'when the joint stock companies were established, the great object was that the shares should be capable of being easily transferred.'

In *Delavenne v. Broadhurst,* (1931) 1 Ch 234, 238) Bemnet J has held that subject to the company's Articles, 'the share-holders has .....the right to transfer his shares without the consent of anybody to any transferee, even though he be a man of straw, provided it is a bona fide transaction in the sense that it is an out and

out disposal of the property without retaining any interest in the property.'

In *Re Discoverers Finance Corpn. Ltd.* (1910) 1 Ch. 207) it was held that a transfer made with the avowed object of escaping liability would be valid in the absence of any collusion between him and the directors.

The provisions relating to transfer of shares can be explained with reference to the following heads:

1. Power of the Board of Directors to refuse transfer (Sec. 44 & 58); and
2. The Companies Act, 2013 (Sec.56).

1. Power of the Board of Directors to refuse transfer (Sec.44 & 58): The Articles of the company may confer on the directors power to refuse any transfer of shares. This power regulates transfer of shares. In case, wide discretionary power is vested to that effect, the directors may refuse any transfer without assigning any reason so long as the power is bona fide in the interest of the company. In such cases, the court will not interfere. Relevant case on this point is –

Re Smith and Fawcett Ltd. – In this instant case, articles of the company conferred on directors wide discretionary power with regard to transfer of shares. F, holding 4001 shares died and his son, S applied to have the deceased's shares registered in his name. The directors accepted to transfer 2001 shares only provided the remaining shares are sold to one of the directors of the company. In an action by S, the court justified the directors action in the interest of the company.

2. Companies Act 2013 (Sec.56): Section 56 of the Companies Act, 2013 and corresponding Sections 108 to 112 of the Companies Act, 1956 lay down the provisions relating to transfer of shares. According to Sec.108.B of the Old Act, a company holding 10% or more of the nominal value of the subscribed equity share capital of any other company proposes to transfer these shares must inform/intimate the same through a statement containing all particulars.

After receiving such information, if the Central Government is satisfied that such transfer results in a change in the Board of Directors of the company and would be prejudicial to the interests of the company and the public, it (Central Government) may direct that:

a) the shares shall not be transferred to the transferee; or

b) where such shares are held in a company engaged in any industry specified under Schedule XIII, such shares shall be transferred to the Central Government or to any corporation owned or controlled by the Central Government for market value of the shares. (Market Value means the value quoted at the stock exchange). In case, the Central Government does not make any direction within 60 days from the date of receipt of the intimation, the power of the Central Government shall cease.

Procedure of Transfer (Sec.56): Section 56 of the Companies Act, 2013 (corresponding Section 108 of the Companies Act, 1956) lays down the procedure for transfer of shares. Section 56 reads as follows:

1. A company shall not register a transfer of securities of the company, or the interest of a member in the company in the case of a company having no share capital, other than the transfer between persons both of whose names are entered as holders of beneficial interest in the records of a depository, unless a proper instrument of transfer, in such form as may be prescribed, duly stamped, dated and executed by or on behalf of the transferor and the transferee and specifying the name, address and occupation, if any, of the transferee has been delivered to the company by the transferor or the transferee within a period of sixty days from the date of execution, along with the certificate relating to the securities, or if no such certificate is in existence, along with the letter of allotment of securities.

   Provided that where the instrument of transfer has been lost or the instrument of transfer has not been delivered within the

prescribed period, the company may register the transfer on such terms as to indemnity as the Board may think fit.

2. Nothing in sub-section (1) shall prejudice the power of the company to register, on receipt of an intimation of transmission of any right to securities by operation of law from any person to whom such right has been transmitted.

3. Where an application is made by the transferor alone and relates to partly paid shares, the transfer shall not be registered, unless the company gives the notice of the application, in such manner as may be prescribed, to the transferee and the transferee gives no objection to the transfer within two weeks from the receipt of notice.

4. Every company shall, unless prohibited by any provision of law or any order of Court, Tribunal or other authority, deliver the certificates of all securities allotted, transferred or transmitted–

   a) Within a period of two months from the date of incorporation, in the case of subscribers to the memorandum.

   b) Within a period of two months from the date of allotment, in the case of any allotment of any of its shares.

   c) Within a period of one month from the date of receipt by the company of the instrument of transfer under sub-section (1) or, as the case may be, of the intimation of transmission under sub-section (2), in the case of a transfer or transmission of securities.

   d) Within a period of six months from the date of allotment in the case of any allotment of debenture.

   Provided that where the securities are dealt with in a depository, the company shall intimate the details of allotment of securities to depository immediately on allotment of such securities.

5. The transfer of any security or other interest of a deceased person in a company made by his legal representative shall,

even if the legal representative is not a holder thereof, be valid as if he had been the holder at the time of the execution of the instrument of transfer.

6. Where any default is made in complying with the provisions of sub-sections (1) to (5), the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees.

7. Without prejudice to any liability under the Depositories Act, 1996, where any depository or depository participant, with an intention to defraud a person, has transferred shares, it shall be liable under Section 447.

Transfer of share to be effective and binding, it must be registered. The procedure for transfer of shares is stated hereunder:

i) Any shareholder or a person whose name appears in the register of members of a company or the legal heir/representative of the deceased member/shareholder is entitled to transfer the shares.

ii) The transfer shall be made by a prescribed instrument of transfer in Form No.SH-4 (The Companies (Share Capital and Debentures) Rules 2014).

iii) The application must be duly stamped, dated and executed on behalf of the transferee. The name, address and occupation of the transferee shall be specified.

iv) The instrument of transfer shall be delivered to the company either by the transferor or transferee within a period of sixty days from the date of execution.

v) It (the instrument of transfer) shall be accompanied by a certificate relating to the securities. If there is no certificate, it shall be accompanied by letter of allotment.

vi) An application for the registration can be made by the transferor or transferee (Sec.56). In case the application made by the

transferor relates to partly paid shares, the company gives notice in Form No.SH-5 (The Companies (Share Capital and Debentures) Rules 2014) to that effect to the transferee. If the transferor makes no objection within two weeks from the date of such notice, the transfer shall be registered. The notice is deemed to be complete, when it is dispatched by prepaid registered post to the transferee.

vii) In case the company, as per the provision of its articles, the same shall be intimated/ informed to the transferor and the transferee.

viii) If the Board of Directors approves the registration by passing a resolution (to that effect) refers the matter to the Secretary for preparation and issue of new share certificate. Accordingly, the names of the old shareholders are replaced by/with the names of new shareholders from the register of members.

Restrictions on Transfer of Shares

Grounds on which a company may refuse to register transfer of shares:- The Board may decline to register the transfer of a share in the following circumstances:

1. In the case of partly paid shares to a transferee whom the Board does not approve.
2. If the company has a lien on the shares.
3. If the instrument of transfer is in respect of more than one class of shares.
4. If the registration fee is not paid.
5. If the instrument of transfer is not accompanied by share certificate.
6. If the instrument of transfer does not bear the require stamp duty and if the stamp has not been cancelled.
7. If the signature of the transferor on the instrument of transfer does not tally with the specimen signature kept by the company.
8. The transfer of shares is prohibited by an order of any Court.

9. The transfer of share is in contravention any law or rule made there under.

10. Any other requirement under the law relating to the registration of transfer has not been complied with.

4. Transmission of Shares (Section 56)

Section 56 of the Companies Act, 2013 (corresponding to Section 109.B of the Companies Act, 1956) provides for the transmission of shares. Transfer of shares may be effected either by the act of parties or by operation of law. The former is called 'transfer of shares', while the latter is called 'transmission of shares'. When a registered shareholder dies, his shares are transferred to the legal heir/ representative. Similarly, when a shareholder becomes insolvent/bankrupt, his shares are transferred to (vested in) the official receiver/assignee. In simple, 'transmission of shares' means, "transfer of shares as a consequence of death or insolvency of the shareholder. Therefore, the executor or successor in case of death of a shareholder or an official receiver/assignee in case of insolvency/ bankruptcy of a shareholder is entitled to have the shares (of the deceased or insolvent shareholder as the case may be) transmitted to him in the register of members. Further, the executor or the successor or official receiver also has the right to transfer the shares.

The articles of companies usually contain a 'transmission clause' as indicated in Article 26 of Table-A giving legal representatives the right either to transfer the shares or have them registered in their name on production of evidence of their representative capacity.

The provisions of Section 58 of the Companies Act, 2013 regarding appeal to Tribunal against refusal of transfer of shares apply *mutatis mutandis* to transmission of shares.

Section 101 of the Companies Act, 2013 further provides that the legal representatives are entitled to receive notices of general meetings of the company even though they are not registered as members but they shall not be entitled to exercise any rights available to members in respect of the shares of the deceased share holder.

However, the difficulty arising in relation to devolution of shares/ debentures due to death of shareholder or debenture holder in absence of legal representative has now been resolved by the provision of nomination of shares under Section 72 of the Companies Act, 2013.

Section 72 further provides that any person who becomes a nominee, upon the production of such evidence as may be, required by the Board of Directors of the company may either elects to be registered himself as holder of the shares/debentures or make such transfer of the shares/debentures as the deceased shareholder or debenture holder could have made.

As stated above, transmission of shares takes place in two ways namely:

1. Transmission on death; and
2. Transmission on Insolvency/Bankruptcy.

1. Transmission on death: When a shareholder dies, his shares vest in his legal representatives. No written instrument is required for the purpose. The company is bound to accept the probate of will or letters of administration. The Companies Act, 2013 confers on the legal representative, the power to further transfer the shares.

2. Transmission on Insolvency/Bankruptcy: When a shareholder is adjudged an insolvent, his shares vest in the official receiver/assignee. The official receiver may hold the shares in his own name or may transfer the same to others/creditors. He can also disclaim the shares, if they contain any liability.

Distinction between transfer and transmission of shares

Following are the notable points of distinction between the transfer of shares and transmission of shares.

Transfer of Shares	Transmission of Shares
1. It is effected by voluntary act of the parties.	1. It is effected by the operation of law (E.g.: Death, Insolvency etc.)
2. It takes place for Considartion.	2. No consideration is Involved.
3. Prescribed instrument of transfer is necessary.	3. There is no such instrument.
4. The transfer is discharged from the liability on the shares after the transfer is complete.	4. Liability on shares if any continues even after the transmission.

5. Share Certificate and Share Warrant

Every company making an allotment of shares or debentures or debenture stock is obliged to deliver to the allottee a certificate of share/debentures etc. within three months after the allotment and in case of transfer of shares, the certificate has to be delivered within two months. The companies Act, 2013 imposes a positive duty on the company to deliver the share certificates within the specified time and in case of any default in this regard, the allottee or the transferee, as the case may be, may give as notice to the company and if the default is not ratified within 10 days of the notice, the allottee can apply to the Company Tribunal. The delivery must be affected in accordance with Section 20 of the Companies Act, 2013.

1. Share Certificate (Section 56)

A share certificate is a document/instrument in writing issued by a company stating that the person, whose name appears therein is a registered holder of specified number of shares in the company and that the shares are fully paid or paid up to the amount specified therein. A share certificate shall be under the seal of the company and signed by at least two Directors and the Secretary. It contains the name, address and occupation of the shareholder. If the shares are of more than one class, it shall specify the class of shares to which it relates.

Delivery of Share Certificate (Section 56(4): Sub-section (4) of Section 56 provides that every company shall, unless prohibited by any provision of law or any order of the Court, Tribunal or other authority, deliver the certificates of all securities/shares allotted, transferred or transmitted:

a) Within two months from the date of incorporation, in the case of subscribers to the memorandum.

b) Within two months from the date of allotment, in case of any allotment of any of its shares.

c) Within one month from the date of receipt by company, of the instrument of transfer or of the intimation of transmission in the case of transmission of securities or shares.

d) Within a period of six months from the date of allotment in the case of allotment of debentures (Sub-section (4) if Section 56 of the Companies Act, 2013).

Where the shares or securities are dealt with in a depository, the company shall intimate the details of allotment of securities/shares to depository immediately on such allotment having been made.

Effect of Share Certificate (Section 46): According to Section 46(1) a share certificate should be issued under a common seal of the company. The Companies (issue of Share Certificate) Rules, 1960 further provide that the share certificates shall be issued:

a) In pursuance of a Board resolution.

b) The certificate should specify the name(s) of the person(s) in whose favour the certificate is issued, and the shares to which it relates and the amount paid up there on.

c) The common seal, if any, of the company on the share certificates should be affixed in the presence of two Directors or persons acting in their behalf under duly registered power of Attorney; and the secretary or some other person appointed by the Board for that purpose.

d) The two directors or their Attorneys may affix their signatures on the certificates by mechanical means such as engraving or lithography but not by means of rubber stamp.

e) All the blank certificate forms should be printed and the printing should be done only on the authority of Board resolution.

f) All the blank forms should be consecutively machine numbered and the forms and engravings, facsimiles and dies relating to the printing of such forms should be kept in safe custody of the secretary or such person as the Board may appoint.

g) Where the shares are listed, the Stock Exchange requirements relating to the format, size and content of the share certificates must also be complied with.

A share certificate issued under the common seal,if any, of the company shall be a *prima facie* evidence of the title of the member to such number of shares as mentioned therein.

2. Share Warrant

A share warrant is a document issued by a public company limited by shares. It states that the bearer (of the warrant) is entitled to that shares specified therein. Share warrants are easily transferable by mere delivery. Registration for the transfer is not necessary. The share warrants are issued under the common seal of the company.

Conditions: A public company limited by shares can issue share warrants provided the following conditions are satisfied:

1. The shares shall be fully paid-up.
2. The Articles of the company shall authorise to issue share warrants.
3. Prior approval of the Central Government shall be obtained.

Distinction between a Share Certificate and a Share Warrant:

Share Certificate	Share Warrant
1. The public companies and private companies can issue share Certificates as well.	1. Only public companies can issue share warrants.
2. Share certificates can be issued in respect of partly paid up shares also.	2. Share warrants can be issued only in respect of fully plaid-up shares.

3. The holder of share certificate is a member of the company.	3. The holder of share warrant is not a member of the company unless the Articles of Association so provide.
4. Transfer requires registration.	4. Registration is not necessary since share warrants are transferred by mere delivery.

6. Lien on Shares

Lien: Meaning: The term 'lien' means, "right to retain the goods or securities till the debt is cleared". Lien is of two kinds namely:

1. Particular or Special Lien; and
2. General Lien.

A **Particular Lien** gives the right to retain possession only of goods in respect of which the charges or dues have arisen. E.g.: Tailor's right to retain the cloths till the stitching charges are paid.

A **General Lien** is one, which gives right to retain possession until the whole balance of the account is paid. It extends not only towards the goods pledged as security but also in respect of others. E.g.: Banker exercises the right of general lien (Sec.171 Indian Contract Act, 1872).

A lien on shares is a contractual lien arising from the contract contained in the articles of the company. A company does not have lien on the shares of its members unless it is expressly conferred to it by the articles. A company is free to provide in its articles that it shall have lien on fully paid shares as regards sums due to it from the shareholders.

A lien is an equitable charge. It gives the company such rights, as it would have had under the general law if the shares had been expressly charged. The Articles of a company may provide that the company shall have a right of lien on the shares of the member for some debt, which may be due from such member to the company. Here the lien means a charge of the company over the shares. To

enforce the right a member could be disallowed from transferring his shares until the debt is paid or his shares could be sold. Before the shares are sold, due notice of the same should be given to the member. The right of lien also extends to the dividends on the shares. It may be noted that the power to exercise the right of lien in one manner or another should be contained in the Articles of the company. If the company has the power, under its Articles, to enforce the lien by the sales of shares, it has also to mention about the appointment of a person who is to execute the instrument of transfer, without which a share cannot be transferred.

A company loses lien under the following two circumstances

1. It registers a transfer of shares subject to the lien of the transferee;
2. A member pledges his shares to a third party as security for a loan and the company has noticed thereof, and then incurs a liability to the company. In such as case, the pledgee has priority over the lien of the company.

Bradford Banking Co. v. Briggs, Son & Co. Ltd., **(1886) 12 App. Cas. 29** – Certain shares of a company were subject to a 'first and paramount lien' by the company. These were given to a bank as security for an overdraft after giving notice to the company. Subsequently the shareholder became indebted to the company-giving rise to a lien in favour of the company. Held, the bank had priority over the company's claim, which arose subsequently.

7. Surrender and Forfeiture of Shares

A Company may invite applications for subscription of shares and the applicants are required to pay the face value of the shares in installments. For instance, if the face value of the share is Rs.10/- the applicant has to pay Rs.2/- on each share against the application, Rs.5/- at the time of allotment, Rs.2/- at the time of first call and the remaining Rs.1/- on second/final call and so on. If a shareholder (allottee) fails to pay against the calls, the company to recover the payment resorts to any one of the following two remedies.

1. To sue him for the amount due, or
2. To forfeit the shares allotted.

Forfeiture of shares: The word 'forfeiture' means, "depriving a person of his property as a penalty for some act or omission (or default of payment)". Forfeiture of shares takes place for non-payment (default) of calls in arrears. It is the compulsory termination of the membership from the 'Register of Members'.

The shares of a member could be forfeited by the company if the power to do so is contained in the articles of the company. The sanction of forfeiture is an effective way of enforcing the payment.

If a member fails to make payment of a valid call or installment of a call within the stipulated time, his share may be forfeited if authorized by the articles of the company. The articles of the company generally empower the directors to forfeit the shares for non-payment of calls by adopting Regulation 28 to 34 of Table-F. The forfeiture of shares can be effected only by means of a resolution of the Board of Directors and after giving due notice to the defaulting shareholders and slightest defect in this regard would invalidate the forfeiture.

The Companies Act, 2013 does not expressly give any statutory right to the companies to forfeit the shares. But the Articles of the company usually empower the directors to forfeit the shares for non-payment of calls. If the Articles are silent, the company may alter the Articles or get the sanction of the Court for the purpose of forfeiting the shares.

In *Madhwa Ram Chandra Kamath v. Canara Banking Corporation* (AIR 1941 Mad. 354), it was held that the authorization of Articles to expel a member is not sufficient to enable the company to deprive the expelled member of his shares.

Condition: Forfeiture, to be valid and enforceable, the following conditions are to be satisfied.

1. The company may forfeit shares in accordance with the Articles of the company subject to the following conditions:

i. the articles relating to forfeiture do not offend against the general law of the land and in particular the Companies Act and public policy; and

ii. that the forfeiture contemplated does not entail or effect a reduction in capital or involve an amount to purchase by the company of its own shares nor does it amount to trafficking in its own shares.

2. Notice – A notice under the authority of the Board of Directors must be given to the defaulting shareholder. Regulation 28 of Table F in Schedule-I provides that if a member fails to pay any call or installment of a call on the day fixed for the payment thereof, the Board may serve a notice on him for payment of the call or installment together with interest (if any). The notice must state

a) the amount payable by the shareholder;

b) the date on which the amount is to be paid (but the date must not be earlier than 14 days from the date when the notice is served) and

c) that if the payment is not made on or before the day stated in the notice, the shares in respect of which the call was made will be liable to be forfeited.

3. Good Faith – The power to forfeit the shares must be exercised by the directors of the company in good faith and for the benefit of the company.

4. Resolution of the Board – If the defaulting shareholder does not make the payment due within the specified time as required by the notice, the directors must pass a resolution forfeiting the shares. In absence of such resolution, the forfeiture shall be invalid.

Effect of Forfeiture: On forfeiture of his shares a person ceases to be a member of the company. The forfeited shares become the property of the company and can be re-issued to another person. Such shares could be sold or otherwise disposed of on such terms and in such manner as the Board thinks fit. Thus there may be sale of such shares at a discount. The member, whose shares are so

forfeited, will continue to be liable for the moneys payable at the time of forfeiture. The purchaser of such shares has also an obligation to pay all what was due at the time of forfeiture, but he has a right to get the benefit of any payments made by its earlier holder.

When a shareholder voluntarily gives back or surrenders his shares to the company, he is said to surrender his shares to the company. In other words, surrender of shares means the return of shares by the shareholder to the company for cancellation voluntarily. The company in normal circumstances cannot accept the surrender of fully paid shares since it amounts to purchase of its own shares by the company, which is illegal and void. The only exception where fully paid up shares may be accepted is when shares are surrendered in exchange for new shares or the same nominal value, but with different rights.

There is no provision either in the Companies Act, 2013 or in Table-F of Schedule-I of the Companies Act, 2013, but the Articles of some companies may allow it. In *MangalSain v. Indian Merchants Bank, Aritsar (*AIR 1928) Lah. 240), it has been held that surrender of shares cannot be accepted without the sanction of the Court, as this would amount to reduction of capital.

Surrendered shares may be re-issued in the same way as forfeited shares. If this is done, no reduction in capital occurs. No consideration is paid by the company in exchange of surrendered shares, since it would amount to purchase of its own shares which is specifically prohibited under Section 67 of the Companies Act, 2013.

Distinction between Surrender and Forfeiture: The legal effect of both the surrender and forfeiture is the same. Both have practically the same effect except for the fact that while surrender is done with the assent of the share-holder, the forfeiture is a proceeding *in invitum* (against a person's will). 'A Company cannot accept a surrender of its shares as every surrender of shares whether fully paid up or not involves a reduction of capital which is unlawful.' Forfeiture is a statutory exception and is the only exception. Following are the notable points of difference between the forfeiture of shares and surrender of shares:

Forfeiture of shares	Surrender of shares
1. Forfeiture of shares is made at the initiative of the company.	1. Surrender of shares is made at the initiative of the shareholder.
2. Forfeiture of shares is a compulsory action. It is forced on the shareholder. He has no choice.	2. Surrender of shares of a voluntary action. Shareholders may take the action at his free will.
3. Forfeiture of shares does not bring any consideration to the defaulting shareholder.	3. Surrender of shares may bring some consideration to the share holder in the shape of return of part of the money paid or remission of interest.
4. Forfeiture of shares is recognized by the Act.	4. Surrender of shares is not recognized by the Act but it has been admitted by the Courts.

8. Bonus Shares

As the name indicates, these shares are allotted in satisfaction of bonus. The word 'Bonus' means "something in form of economic benefit, given in addition to what is usually or strictly due (i.e. paid in excess of what out to be paid)'. Issue of bonus shares is called 'capitalization of profits'. Bonus issue is not an offer. It is a capitalization issue and is also known as 'scrip issue'. Bonus shares shall be fully paid up shares. These fully paid up shares so issued to the old shareholders of the company are known as 'Bonus Shares'.

Sometimes huge profits are accumulated and the company with the intention to distribute these profits and instead of paying the dividends or bonus in cash, the company issues fully paid up new shares to its members or applies the dividends (or bonus) belonging to the shareholders in the payment of the unpaid value of the shares already held by them.

Sometimes 'Bonus' is something given in addition to what is usually or strictly due. If the Articles of the company permit, it may

convert a part of the reserves into share capital by issuing fully paid bonus shares to the existing shareholders.

These shares can only be issued if:

a) the company has been authorised by its articles to issue such shares; and

b) the company has sufficient undistributed profits.

A return of the issue of bonus shares stating their number and nominal amount is required to be filed by the company with the Registrar of Companies.

Lecture–VIII
SHARE CAPITAL

This lecture covers –

1. Share Capital: Meaning and Kinds.
2. Alteration of Capital (Sec.94).
3. Reduction of Share Capital (Ss.100-105).
4. Issue of Shares at Premium (Sec.78).
5. Issue of Shares at Discount (Sec.79).
6. Issue of Sweat Equity Shares (Sec.79.A).

1. Share Capital: Meaning and Kinds

Meaning: The words 'Capital' and 'Share Capital' are synonymous. The word 'capital' has several meanings. It means 'a particular amount, invested to start a business'. Capital may be used to mean capital goods that is, the tools of production, the money available for investment, or invested, the discounted value of the future income to be received from an investment, the real or money value of total assets, money or property used for the production of wealth, sum total of corporate stock. Capital is accumulated goods, possessions and assets, used for the production of profits and wealth.

'Share capital on the other hand' means "Share Capital" in respect of a company limited by shares. In other words, investment of capital in a public limited company is called 'share capital.' It is raised by a company by issue of shares to the public.

The Memorandum of Association of a company contains a capital clause providing for the amount of capital dividend into different shares, with which the company is to be registered. Share capital means the capital raised by a company by the issue of shares. The word 'capital' in connection with a company is used in several senses, it may mean authorised, issued and subscribed, or paid up or reserve capital of the company.

Kinds of Capital: The term 'capital' is used in different senses, namely –

i) Authorised or Nominal or Registered Capital.
ii) Issued Capital.
iii) Subscribed Capital.
iv) Called-up Capital.
v) Paid-up Capital.
vi) Uncalled Capital.
vii) Reserve Capital.
viii) Fixed capital; and
ix) Circulating Capital.

i) Authorised or Nominal Capital: In case of a company limited by shares the memorandum has to mention the amount of share capital with which the company proposes to be registered, and the division thereof into shares of a fixed amount (Sec.4). It is the maximum capital, which the company will have during its lifetime unless it is increased. For instance, a company is authorised to issue 500000 shares of Rs.100/- each. Its authorised capital is Rs.5,00,00,000/-. It is the maximum limit, beyond which the company cannot call for.

ii) Issued Capital: Issued capital is the nominal value of the shares, which are offered to the public for subscription. A Company does not normally issue all its capital at once, so that issued capital in such a case is less than the authorised capital. The issued capital can never exceed the authorised capital; it can at the most be equal to the authorised capital which is the case when all the shares have been issued to the public. For instance, out of the authorised capital of Rs.5,00,00,000/- the company may issue 25000 shares of Rs.100/- i.e. Rs.2,50,00,000/-.

iii) Subscribed Capital: It is the nominal value of the shares, which have been subscribed. For instance, out of the issued capital Rs.2,50,00,000/- if the capital worth Rs.20,00,000/- is subscribed i.e. for 20000 shares, the subscribed capital is Rs.2,00,00,000/-.

iv) Called-up Capital: This is that part of the issued capital, which has been called up on the shares. In the above example, out of the subscribed capital of Rs.2,00,00,000/- if the subscribers (allottees of shares) are required to pay by 1st call, 2nd call etc., it is called called-up capital. It may be Rs.2,00,00,000/- or less than Rs.2,00,00,000/- say Rs.1,50,00,000/-.

v) Paid-up Capital: The actual amount paid up or credited as paid up on the shares subscribed for and allotted is the paid up capital. Suppose, the company called for payment of Rs.1,50,00,000/- and received payment of Rs.1,20,00,000/- it is called paid-up capital.

vi) Uncalled Capital: This is the remainder of the issued capital, which has not been called. The company may call this amount any time but this is subject to the terms of issue of shares and the provisions of the Articles. E.g.: A Company is registered with a capital of Rs.1,00,00,000/- divided into 1,00,000 shares of Rs.100 each. The authorised capital of the company in such a case is Rs.10,00,000/- The company offers 80,000 shares to the public which takes them up. The issued capital of the company is Rs.8,00,000 The company calls up only Rs.60/- per share. In such a case, the called up capital is Rs.4,80,000/- and the uncalled capital is Rs.32,000.

vii) Reserve Capital: This is the part of the uncalled capital which cannot be called except in the event and for the purpose of the winding up of the company. A limited company may, by special resolution determine that any portion of its share capital which has not been already called up, shall not be capable of being called up, except in the event and for the purpose of the company being wound up and thereupon that portion of its share capital shall not be capable of being called up except in that event and for those purposes. A Company is not entitled to create any charge on its share capital. Reserve capital cannot be converted into ordinary capital except with the leave of the Court/Tribunal.

viii) Fixed Capital: This is the property acquired by the company with the intention to retain it and employed in the business

of the company permanently and not to resell it, E.g.: buildings and machineries etc.

ix) Circulating Capital: This is the property, acquired or produced by the company with the intention to resell it at a profit, E.g.: goods produced by the company for sale, ordinary merchandise, etc.

Kinds of Share Capital: The capital of a company is divided into shares of a fixed amount. The shares may be of one class/kind or different kinds covering different rights and benefits as determined by the Memorandum or Articles of the Company. The new Under Section 43 provides that the share capital of a company limited by shares shall be of two kinds only, namely –

a) equity share capital:
   i) with voting rights; or
   ii) with differential rights as to dividend, voting or otherwise in accordance with such rules and subject to such conditions as may be prescribed.

b) preference share capital.

a) Equity Share Capital: Equity Share Capital means all share capital which is not preference share capital

Share capital with differential rights: It means a share that is issued with differential rights in accordance with the provisions of Sec.43 of Companies Act, 2013 and rules prescribed thereunder.

b) Preference share capital: Preference share capital means that part of the share capital which fulfils the following requirements, namely –

a) During the continuance of the company it will carry preferential right in respect of dividends; and

b) In the event of winding up of the company it will have a preferential right as to the repayment of the paid up capital.

2. Alteration of Capital (Section 61)

Section 61 of the Companies Act, 2013 (Corresponding to Section 94 of the Companies Act, 1956) provides for the alteration of share capital. It reads as follows –

Power of limited company to alter its share capital— (*1*) A limited company having a share capital may, if so authorised by its articles, alter its memorandum in its general meeting to:

(a) increase its authorised share capital by such amount as it thinks expedient;

(b) consolidate and divide all or any of its share capital into shares of a larger amount than its existing shares:

Provided that no consolidation and division which results in changes in the voting percentage of shareholders shall take effect unless it is approved by the Tribunal on an application made in the prescribed manner;

(c) convert all or any of its fully paid-up shares into stock, and reconvert that stock into fully paid-up shares of any denomination;

(d) sub-divide its shares, or any of them, into shares of smaller amount than is fixed by the memorandum, so, however, that in the sub-division the proportion between the amount paid and the amount, if any, unpaid on each reduced share shall be the same as it was in the case of the share from which the reduced share is derived;

(e) cancel shares which, at the date of the passing of the resolution in that behalf, have not been taken or agreed to be taken by any person, and diminish the amount of its share capital by the amount of the shares so cancelled.

(2) The cancellation of shares under sub-section (1) shall not be deemed to be a reduction of share capital.

If a company is so authorised by its Articles it may alter its share capital in the following ways:

1. Increase its share capital by issuing new shares.
2. Consolidate and divide all or any of its share capital of larger amount than its existing ones.
3. Convert all or any of its fully paid up shares into stock, and reconvert that stock into fully paid up shares of any denomination.
4. Sub-divide all or any of its shares into shares of a smaller amount; and
5. Cancel such shares, which have not been taken up, and reduce its share capital accordingly. Such cancellation of the shares shall not be deemed to be reduction of share capital within the meaning of the Act.

The power of alteration of the capital shall be exercised by the company in general meeting and shall not require to be confirmed by the Court/Tribunal. Notice of the above should be given to the Registrar of Companies within 30 days (Sec.64).

3. Reduction of Share Capital (Section-66)

Section 66 of the Companies Act, 2013 (Corresponding Sections 100 to 105 of the Companies Act, 1956) provides for the reduction of share capital. Section 66 reads as follows:

(1) Subject to confirmation by the Tribunal on an application by the company, a company limited by shares or limited by guarantee and having a share capital may, by a special resolution, reduce the share capital in any manner and in particular, may:

(a) extinguish or reduce the liability on any of its shares in respect of the share capital not paid-up; or

(b) either with or without extinguishing or reducing liability on any of its shares:

   (i) cancel any paid-up share capital which is lost or is unrepresented by available assets; or

   (ii) pay off any paid-up share capital which is in excess of the wants of the company,

alter its memorandum by reducing the amount of its share capital and of its shares accordingly:

Provided that no such reduction shall be made if the company is in arrears in the repayment of any deposits accepted by it, either before or after the commencement of this Act, or the interest payable thereon.

(2) The Tribunal shall give notice of every application made to it under sub-section (1) to the Central Government, Registrar and to the Securities and Exchange Board, in the case of listed companies, and the creditors of the company and shall take into consideration the representations, if any, made to it by that Government, Registrar, the Securities and Exchange Board and the creditors within a period of three months from the date of receipt of the notice:

Provided that where no representation has been received from the Central Government, Registrar, the Securities and Exchange Board or the creditors within the said period, it shall be presumed that they have no objection to the reduction.

(3) The Tribunal may, if it is satisfied that the debt or claim of every creditor of the company has been discharged or determined or has been secured or his consent is obtained, make an order confirming the reduction of share capital on such terms and conditions as it deems fit:

Provided that no application for reduction of share capital shall be sanctioned by the Tribunal unless the accounting treatment, proposed by the company for such reduction is in conformity with the accounting standards specified in section 133 or any other provision of this Act and a certificate to that effect by the company's auditor has been filed with the Tribunal.

(4) The order of confirmation of the reduction of share capital by the Tribunal under sub-section (3) shall be published by the company in such manner as the Tribunal may direct.

(5) The company shall deliver a certified copy of the order of the Tribunal under sub-section (3) and of a minute approved by the Tribunal showing:

(a) the amount of share capital;

(b) the number of shares into which it is to be divided;

(c) the amount of each share; and

(d) the amount, if any, at the date of registration deemed to be paid-up on each share,

to the Registrar within thirty days of the receipt of the copy of the order, who shall register the same and issue a certificate to that effect.

(6) Nothing in this section shall apply to buy-back of its own securities by a company under section 68.

(7) A member of the company, past or present, shall not be liable to any call or contribution in respect of any share held by him exceeding the amount of difference, if any, between the amount paid on the share, or reduced amount, if any, which is to be deemed to have been paid thereon, as the case may be, and the amount of the share as fixed by the order of reduction.

(8) Where the name of any creditor entitled to object to the reduction of share capital under this section is, by reason of his ignorance of the proceedings for reduction or of their nature and effect with respect to his debt or claim, not entered on the list of creditors, and after such reduction, the company is unable, within the meaning of sub-section (2) of section 271, to pay the amount of his debt or claim:

(a) every person, who was a member of the company on the date of the registration of the order for reduction by the Registrar, shall be liable to contribute to the payment of that debt or claim, an amount not exceeding the amount which he would have been liable to contribute if the company had commenced winding up on the day immediately before the said date; and

(b) if the company is wound up, the Tribunal may, on the application of any such creditor and proof of his ignorance as aforesaid, if it thinks fit, settle a list of persons so liable to contribute, and make and enforce calls and orders on the contributories settled

on the list, as if they were ordinary contributories in a winding up.

(9) Nothing in sub-section (8) shall affect the rights of the contributories among themselves.

(10) If any officer of the company:

(a) knowingly conceals the name of any creditor entitled to object to the reduction;

(b) knowingly misrepresents the nature or amount of the debt or claim of any creditor; or

(c) abets or is privy to any such concealment or misrepresentation as aforesaid,

he shall be liable under section 447.

(11) If a company fails to comply with the provisions of sub-section (4), it shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees.

It is said that conservation of capital is one of the main principles of company law. The share capital of a company is the only security on which the creditors rely. Any reduction of capital diminishes the fund out of which they are to be paid.

Since reduction of capital affects the company, the shareholders and the creditors, it is considered as a serious matter and is unlawful except when sanctioned by the Tribunal.

The *Supreme Court in Kartikeya Sarabhai v. The Commissioner of Income Tax* (AIR 1997 SC 3794) held that when as a result of the reducing of the face value of the share, the share capital is reduced, the right of the preference shareholder to the dividend or his share capital and the right to share in the distribution of the net assets upon liquidation is extinguished proportionately to the extent of reduction in the face value of the share and the value of the vote of the shareholder in the event of there being a poll would stand considerably reduced.

But sometimes, there may be a genuine necessity for the reduction of capital. Therefore a closely fenced power is given by Section 66 of the Act, according to which a company limited by shares or a company limited by guarantee having a share capital may reduce its capital in any way i.e. it may –

i) By extinguishing or reducing the liability in respect of unpaid share capital, or

ii) By way of either without reducing or extinguishing the liability in respect of paid up share capital which was lost and unrepresented by assets, or

iii) By way of payment of any paid up share capital which was in excess, either with or without reducing or extinguishing the liability.

Where a company has passed a special resolution for reducing share capital it may apply, by petition, to the Tribunal for an order confirming the reduction. The confirmation by the Tribunal is required so that the interests of the creditors and the shareholders can be protected. When there is extinction or reduction in the liability of its members in respect of the uncalled capital, or there is payment to any shareholder of the paid-up share capital, the interests of the creditors are likely to object to the reduction of capital. If any creditor raises an objection to the reduction of capital, the Tribunal may, if it thinks fit, dispense with the consent of that creditor, on the company securing payment of his debt.

The prescribed majority of the members are to decide as to whether there should be reduction, and if so, in what manner and to what extent if the interests of the creditors and the investing public are safeguarded, and there is just and equitable treatment of the shareholders, the Tribunal will confirm the reduction.

If the Tribunal is satisfied, it may make an order confirming the reduction on such terms and conditions, as it thinks fit. In its order the Tribunal may also direct that the company will and the word 'and reduced' at the end of its name for a specific period, and publish the reasons for the reduction. The fact of the Tribunal order

confirming the reduction has to be got registered with the Registrar. After the reduction the liability of a member is to pay the difference between what he has already paid, or is deemed to have paid, and the amount of the share as fixed on reduction.

4. Issue of Shares at Premium (Section 52)

Section 52 of the Companies Act, 2013 (Corresponding Section 78 of the Companies Act, 1956) provides for issue of shares at premium. It runs as follows –

Application of premiums received on issue of shares— (1) Where a company issues shares at a premium, whether for cash or otherwise, a sum equal to the aggregate amount of the premium received on those shares shall be transferred to a "securities premium account" and the provisions of this Act relating to reduction of share capital of a company shall, except as provided in this section, apply as if the securities premium account were the paid-up share capital of the company.

(2) Notwithstanding anything contained in sub-section (*1*), the securities premium account may be applied by the company:

(a) towards the issue of unissued shares of the company to the members of the company as fully paid bonus shares;

(b) in writing off the preliminary expenses of the company;

(c) in writing off the expenses of, or the commission paid or discount allowed on, any issue of shares or debentures of the company;

(d) in providing for the premium payable on the redemption of any redeemable preference shares or of any debentures of the company; or

(e) for the purchase of its own shares or other securities under section 68.

(3) The securities premium account may, notwithstanding anything contained in sub-sections (1) and (2), be applied by such class of companies, as may be prescribed and whose financial statement comply with the accounting standards prescribed for such class of companies under section 133:

(a) in paying up unissued equity shares of the company to be issued to members of the company as fully paid bonus shares; or

(b) in writing off the expenses of or the commission paid or discount allowed on any issue of equity shares of the company; or

(c) for the purchase of its own shares or other securities under section 68.

A public limited company may issue shares in excess of the face value of its shares, when it is hopeful/confident in view of its good will reputation in the market. The expression 'premium' is not defined in the Companies Act, 2013. It means the value of any advantage measurable in terms of money which is conferred on the company and which is over and above the cash payment on the shares issued by the company. The power of the company to issue shares at a premium need not be taken in the Articles of the company.

A Company may issue its shares at a premium, i.e. more than its nominal value. For instance, when the nominal value of the share is Rs.10/- a company may issue the same at a premium of Rs.20/- i.e. it may take the payment of Rs.30/- per share. Where a company issues shares at a premium, whether for cash or otherwise, a sum equal to aggregate amount of the premium has to be transferred to an account to be called as' the share premium account'.

The share premium account can be utilised by the company for the following purposes:

i. For issuing bonus shares to its members.

ii. For writing off the preliminary expenses of the company.

iii. For writing off the expenses of, or the commission paid or discount allowed on any issue of shares or debentures of the company.

iv. For providing for the premium payable on the redemption of any redeemable preference shares or debentures of the company.

Can different premium be charged on issue of shares? When shares are issued to the public at a premium, ordinarily premium at

a uniform rate is charged from all the applicants for shares. But that is not because the law contains a prohibition against charging different premium. The right of a company to charge varying premium in respect of blocks of shares having the same rights issued under different resolutions is not denied, and on principle there is no objection to the charging of varying rates of premium for shares issued under a single resolution, if all the parties concerned agree [*Commissioner of Income Tax v. Standard Vaccum Oil Co.*, AIR (1966) SC 1393].

5. Prohibition on Issue of Shares at Discount (Sec. 53)

In case there is no demand for the shares issued by a company, the company may resort to employ underwriters by offering extra commission or the company may issue the shares at the discount i.e. at less than the nominal value. Section 79 of the Companies Act, 1956 made provision for issue of shares at discount i.e. less than the face value of the shares. However, Section 53 of the Companies Act, 2013 (which came into force w.e.f. 01-04-2014) prohibits issue of shares at discount. Section 53 reads as follows –

(1) Except as provided in section 54, a company shall not issue shares at a discount.

(2) Any share issued by a company at a discounted price shall be void.

(3) Where any company fails to comply with the provisions of this section, such company and every officer who is in default shall be liable to a penalty which may extend to an amount equal to the amount raised through the issue of shares at a discount or five lakh rupees, whichever is less, and the company shall also be liable to refund all monies received with interest at the rate of twelve per cent. per annum from the date of issue of such shares to the persons to whom such shares have been issued.

However, a company may issue shares at discount to its creditors when its debt is converted into shares in pursuance of any statutory plans or restructuring scheme in accordance with RBI Guidelines or Banking Regulation Act, 1949.

6. Issue of Sweat Equity Shares (Section 54)

Section 54 of the Companies Act, 2013 provides for the issue of 'Sweat Equity Shares'. The corresponding section of the Old Act i.e. the Companies Act, 1956 is 79.A, which was inserted in the Companies Act, 1956 by the Companies (Amendment) Ordinance, 1998. It allows issue of sweat equity to directors and employees. Section 54 reads as follows –

(1) Notwithstanding anything contained in section 53, a company may issue sweat equity shares of a class of shares already issued, if the following conditions are fulfilled, namely:

(a) the issue is authorised by a special resolution passed by the company;

(b) the resolution specifies the number of shares, the current market price, consideration, if any, and the class or classes of directors or employees to whom such equity shares are to be issued;

(c) [xxx]

(d) where the equity shares of the company are listed on a recognised stock exchange, the sweat equity shares are issued in accordance with the regulations made by the Securities and Exchange Board in this behalf and if they are not so listed, the sweat equity shares are issued in accordance with such rules as may be prescribed.

(2) The rights, limitations, restrictions and provisions as are for the time being applicable to equity shares shall be applicable to the sweat equity shares issued under this section and the holders of such shares shall rank *pari passu* with other equity shareholders.

'Sweat equity shares' means, "shares issued at a discount or for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.

A Company may issue sweat equity shares of a class of shares already issued subject to the following conditions:

a) The issue of sweat equity shares should be allowed by a resolution passed by the company in the general meeting.

b) The resolution should specify the number of shares, their value and the class or classes of directors or employees to whom such equity shares are to be issued.

c) Not less than one year has at the date elapsed since the date on which the company was entitled to commence business; and

d) The sweat equity shares are issued in accordance with the regulations made by the S.E.B.I. in this behalf.

The sweat equity shares shall be subject to all the limitations, restrictions and provisions relating to equity shares.

Lecture-IX
MEMBERSHIP OF COMPANY

This lecture covers —

1. Member: Meaning and Definition.
2. Who can become a Member.
3. How to become a Member.
4. Benami Shareholders (Sec.187-C).
5. Termination or Cessation of Membership; and
6. Rights and Liabilities of Members.

1. Member: Meaning and Definition

Meaning: A public limited company is composed of a group of persons called members or shareholders. In case of a company limited by shares, the persons, whose names are put on the Register of members, are the members of the company. The subscribers of the Memorandum of Association or those (atleast seven persons in case of a public limited company and two persons in case of a private limited company and one person in case of one person company), who sign in the subscription clause of the Memo shall be deemed to have become members on registration of the company and their names shall be entered in the Register of members. In other words, any person, whether he is a shareholder or not, whose name appears in the Register of members is deemed to be a member of the company.

The terms 'member' and shareholder are synonymous and are used interchangeably. A member is one, whose name appears in the register of members. While shareholder is a person, who holds certain shares of the company. The shareholder or any other person, who agrees/undertakes in writing to become a member and whose name is entered in the register of members, shall be a member of the company.

Every share holder does not become a member automatically unless he/she applies for membership and the name is entered in the register of members. Similarly, a person need not be a shareholder to become a member.

One who subscribes to the memorandum of a company automatically becomes a member on the registration of the company. Neither application form, nor allotment of, shares is necessary.

In *Official Liquidator v. Suleman Bhai* (AIR 1955 MB 166), where a person subscribed a company's memorandum for 200 shares he was held liable in the winding up of the company for all the 200, although he had taken up only 20.

Definition (Sec.2(55)): Section 2(55) of the Companies Act, 2013 (Corresponding to Section 41 of the Companies Act, 1956) defines a member in the following words:

(i) the subscriber to the memorandum of the company who shall be deemed to have agreed to become member of the company, and on its registration, shall be entered as member in its register of members;

(ii) every other person who agrees in writing to become a member of the company and whose name is entered in the register of members of the company;

(iii) every person holding shares of the company and whose name is entered as a beneficial owner in the records of a depository;

Thus, to constitute member, the following conditions are to be satisfied;

i. There must be an agreement in writing to take/purchase shares of the company; and

ii. The name (of the shareholder) shall be entered in the register of members.

Member v. Shareholder: A member and a shareholder can be differentiated on the following grounds:

1. A person who owns a share warrant is not a member since his name does not appear in the Register of members maintained by the company. He is a shareholder only.
2. A legal representative of a deceased member is a shareholder but not a member, till he applies for registration and his name is entered in the Register of members.
3. A registered member may not be a shareholder, since a company limited by guaranteed and not having the share capital does have members but not shareholders. But registered share holder is a member since his name appears in the register of members maintained by the company.

2. Who can become a Member

The Companies Act, 1956, prescribes no qualifications to become a member of a company. Since the membership with a company is nothing but a contract between two parties, the conditions under Sec. 10 and 11 of the Indian Contract Act, 1872 for validity and competence respectively of a contract must be complied with; In other words membership/contract with a company to be valid, the following two conditions are to be satisfied.

i. The contract must be a valid contract under Section 10 of the Indian Contract Act, 1872; and

ii. The person entering into contract with a company must be competent to contract Under Sec.11 of the Indian Contract Act, 1872 [i.e. he (a) must be a major; (b) must be of sound mind; and (c) must not have been disqualified to contract by the law in force].

1. Minor: a minor being incompetent to contract, cannot become a member of a company since a contract entered into with minor is void *ab initio*.

In *PalaniappaMudaliar v. Official Liquidator; Pasupathi Bank Ltd* (AIR 1942 Mad. 470) shares were allotted by a company is a minor under an application signed by her father as guardian. Subsequently it went into liquidation. It was held that the agreement

with minor was void and the father, who signed the application, could not be deemed to have contracted for the shares, and thus could not be placed on the list of contributories.

If the director allot shares to a minor in response to his application, without knowing that he was a minor and enter his name on the register of members, as soon as the company comes to know of this fact, it can cancel the allotment and strike off the name of the minor from the register of members. But the company must refund the entire money to the minor which it obtained in relation to the shares allotted. However, in latest decisions a minor been permitted to be a member.

The minor may also repudiate the allotment any time during his minority. If the allotment is not repudiated by the minor, his name appears in the register of members, he is not liable to pay any call during his minority. On obtaining majority, if he does not want to continue as a member he must repudiate his liability on the shares within a reasonable time. If he does not do so, he will become liable on a member as the ground of estoppels.

In *Dewan Singh v. Minerva Films* (AIR 1952 Pat. 106) the Punjab High Court held that there is no legal bar to minor becoming member of a company by acquiring shares (by way of transfer) provided the shares are fully paid up and no further obligation or liability is attached to them.

In *FazulbhoyZaffar v. Credit Bank of India Ltd.* (AIR 1914 Bom. 128), it has been held by the Companies Tribunal (now abolished) that if a minor's name is entered in the register of members as an allottee, the company cannot afterwards *suomotu* delete his name and he is entitled to rectification, if the company does so. Similar judgment was given in *Navin Chandra v. Gordhandas* (1967) 1 Comp. LJ 82).

An agreement in writing for a minor to become a member may be signed on behalf of the minor by his lawful guardian and the registration of a transfer of shares in the name of the minor, acting through his or her guardian, specially where the shares are fully paid, cannot be refused on the ground of the transferee being a minor.

In *Golcunda Industries v. Registrar of Companies* (AIR 1968 Delhi 170), the Delhi High Court has held that the Registrar of Companies cannot refuse to accept a return as to allotment in which a minor is shown as an allottee. The Court agreed that the whole law relating to a minor joining a company is still uncertain.

2. Persons of unsound mind and insolvents: Besides minors, other disqualified would include, for example, persons of unsound mind and insolvents. The position of a person of unsound mind is akin to that of a minor. So far an insolvent is concerned, he may be a member of a company. In *Morgan v. Gray,* (1953) Ch. 83), it has been held that so long as his name appears in the register of members, he is a member and is entitled to vote even though his shares vest in the Official Assignee or Receiver.

3. Insolvent: An insolvent may not become a member of a company but for an existing member of the company has become an insolvent, he shall remain member so long as his name is on the register of members, notwithstanding his insolvency, unless article provide otherwise. His Official Assignee or Receiver may, however, be entitled to be registered as a member if he so desires. An insolvent is therefore entitled to vote or give proxies in respect of the shares held by him even though he no longer has any beneficial interest in them, but he has to exercise his voting right as directed by the Official Assignee or Receiver.

4. Partnership Firm: A partnership firm may hold shares in a company in the individual names of partners or as joint share holders. As an unincorporated association, a firm is not a person and as such it cannot be entered as a member in the register of members.

According to Section 8(3) of Companies Act, 2013 'a firm may be a member of the company registered under this section.'

5. Foreigner: A foreigner may become a member of a company, but if at any time he becomes an alien enemy, his rights as a member of the company are suspended.

6. Company as a Member: A company, being a legal person can become member of another company if its memorandum empowers it to invest money in shares.

According to Section 67(1) of the Companies Act, 2013, no company limited by shares or by guarantee and having a share capital shall have power to buy its own shares unless the consequent reduction of share capital is effected under the provisions of this Act.

Purchase by a company of its own shares is illegal because it involves return of capital to the shareholders, which amounts to reduction of the Company's capital without the consent of the Court.

Trevor v. Whitworth, (1887) 12 App. Cas. 409– A Company was authorised by its Articles to purchase its own shares. W sold his shares to the company. Before the full price of the shares was paid, the company went into liquidation. W claimed to prove in the liquidation for the balance of the price of the shares. Held, the transaction was ultra vires the company as the company had no power to purchase its own shares, and hence the claim of W failed.

In view of new Sec.68 [corresponding to Section 77.A, which was inserted to the Companies Act, 1956 by the Companies (Amendment) Act, 1999] a company can buy-back its own shares, notwithstanding anything contained in Sec.67.

3. How to become a Member

A person can become a member of a company in any one of the following ways:

1. By Subscribing to the Memorandum; or
2. By Application and Registration; or
3. By Qualification Shares; or
4. By Beneficial Ownership; or
5. By Transfer of Shares; or
6. By Transmission of Shares, and
7. By Acquiescence and estoppel.

1. By Subscribing to the Membership: The memorandum of each company contains a subscription clause and all the persons who wish to be formed into a company are required to subscribe

their names to the memorandum with their address and the number of shares each of them has agreed to take. All these subscribers of memorandum are deemed to have agreed to become members of the company and on the registration of the company their names are automatically entered as members in the company's register of members. Thus, a subscriber of memorandum becomes a member of the company by the very fact of subscription and neither application form nor allotment of shares in his name is required to make him a member of the company. A person who signs the memorandum enters into a contract with the company to take the number of shares written opposite his name and he cannot repudiate his contract on the ground of misrepresentation.

Official Liquidator v. Suleman Bhai, AIR (1955) MB 116 – S subscribed to a company's Memorandum for 200 shares, but actually he took only 20 shares. Held, he was liable in the winding up of the company for all the 200 shares, as he became a member by the very fact of subscription.

2. By Application and Registration: A person who agrees in writing to become a member of a company and whose name is entered into the company's register of members is treated as a member of the company. A contract to take shares is usually made by application and allotment. A person who wishes to take shares of a company is required to apply for such number of shares as he desires to take and if his application is accepted by the company by allotting shares in his name and the notice thereof is communicated to the applicant, the contract to take shares will become complete entitling the allottee or applicant to the membership of the company. However, the allotment merely entitled the allottee to become a member of the company but he does not become a member until his name is entered in company's register of members. If his name is entered on the register of members, he will become a member of the company but so long as his name is not entered on the register, he cannot be treated as a member of the company.

3. By Beneficial Ownership: Every person holding equity share capital of a company and whose name is entered as beneficial

owner in the records of the depository shall be deemed to be a member of the concerned company.

4. By Transfer of Shares: Shares in a company are movable property as provided in Section 44 of Companies, Act, 2013 and are therefore, transferable in the manner as provided in the articles of the company and in accordance with the provisions of Section 56 of the Act. A person may purchase shares of a company in the open market or from an existing member and then apply to the company for inclusion of his name as a member in the company's register of members. However, if the name of a member of the company is struck off from the register due to a forged transfer, he shall not cease to be a member of the company in such a case. It must be stated that existence of the name in the register of members of the company is only a *prima facie* evidence of the membership and not the conclusive evidence of it.

5. By Transmission of Shares: Transfer of shares takes place in two ways namely, (i) act of parties, and (ii) operation of law.Thus, the property in any shares may devolve on a person by operation of law. For example on the death of a person, his legal representative may become entitled to the shares held by such person. This is transmission of shares to the legal representative. When such legal representative gets the shares registered in his own name, he becomes the member of the company.

6. By Acquiescence and Estoppel: The expression 'estoppel' is derived from the French word 'estoup', which means, "shut the mouth". It is based on the principle of equity and good conscience. It (estoppel) is enshrined in the Latin maxim "Alleganscontrariaaudierdus", which means, 'a man alleging contradictory facts ought not to be heard'. The object of the principle of estoppel is to prevent fraud and to manifest good faith among the parties.

A person will be deemed to be a member of a company if he allows his name to be on the company's register of members or otherwise he holds himself out or allows himself to be held out as a member of the company and during winding up of the company he

will be liable as a contributory. However, if his name has been entered in the register of members improperly, he can escape liability by taking prompt action to have his name removed from the register of members.

7. Depositories Act, 1996: Consequent to the enforcement of Depositories Act, 1996, Section 2(55) of the Companies Act, 2013 provides that a person who is the holder of Company's equity shares and whose name is recorded in the record of depositories as beneficial shareholder, will be a member of the Company. In other words, the holder of shares through depository will acquire membership of the company. But a person who merely holds shares in demat form shall not be treated as a member of the company because his name is not registered in the Register of Members as member of the company.

Register of Members (Sec.88): According to Section 88 of the Companies Act, 2013 (corresponding to Section 150 of the Companies Act, 1956), every company shall maintain a register of members. It reads as follows –

1. Every company shall keep and maintain the following registers in such form and in such manner as may be prescribed, namely:

a) Register of members indicating separately for each class of equity and preference shares held by each member residing in or out side India.

b) Register of debenture holders, and

c) Register of any other security holders.

2. Every register maintained under sub-section (1) shall include an index of the names included therein.

3. The register and index of beneficial owners maintained by a depository under Section 11 of the Depositories Act, 1996, shall be deemed to be the corresponding register and index for the purpose of this Act.

4. A company may, if so authorized by its articles, keep in any country outside India, in such manner as may be prescribed, a part

of the register referred to in sub-section (1), called 'foreign register' containing the names and particulars of the members, debenture holders, other security holders or beneficial owners residing outside India.

5. If a company does not maintain a register of members or debenture holders or other security holders or fails to maintain them in accordance with the provisions of sub-section (1) or sub-section (2), the company and every officer of the company who is in default shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees and where the failure is a continuing one, with a further fine which may extend to one thousand rupees for every day, after the first during which the failure continues.

Every company shall keep a register of its members and enter therein the following particulars:

a) The name and address, and the occupation of each member.

b) In the case of a company having a share capital, the shares held by each member distinguishing each share by its number except where such shares are held with a depository and the amount paid, or agreed to be paid, on those shares.

c) The date at which each person was entered in the register as a member.

d) The date at which any person ceased to be a member.

If the company has converted any of its shares into stock and given notices of the conversion to the Registrar, the register shall show the amount of stock held by each of the members instead of the shares.

Penalty: If any default is made in maintaining the register in the above manner, the company and every officer of the company, who is in default, shall be punishable wit fine which shall not be less than fifty thousand rupees but which may extend to three lakh rupees and if the failure continues, a further fine of one thousand rupees per day during the continuance of the failure.

Index of Members (Sec.88): Every company with more than 50 members shall keep an index of members along with the register. The register itself may be kept in such a way as to constitute an index. The index may also be in the form of a card index. Any alteration in the register of members shall be noted in the index within 14 days of the alteration. The index shall, in respect of each member, contain a sufficient indication to enable the entries relating to that member in the register to be readily found. The index shall, at all times, be kept at the same place in the register of members.

Register and index of beneficial owners (Sec.88): Section 88 of the Companies Act, 2013 (Corresponding to Section 152.A,inserted by the Depositories Act, 1996) envisages the maintenance of the Register and Index of beneficial owners. It has to be maintained by a depository under Sec.11 of the Depositories Act, 1996 shall be deemed to be an index of members and register and index of debenture-holders, as the case may be, for the purpose of this Act.

4. Benami Shareholders (Section 89)

Section 89 of the Companies Act, 2013 (Corresponding to Section 187.C of the Companies Act, 1956) speaks about the 'declaration in respect of beneficial interest in any share. It reads as follows –

Declaration in respect of beneficial interest in any share— (1) Where the name of a person is entered in the register of members of a company as the holder of shares in that company but who does not hold the beneficial interest in such shares, such person shall make a declaration within such time and in such form as may be prescribed to the company specifying the name and other particulars of the person who holds the beneficial interest in such shares.

(2) Every person who holds or acquires a beneficial interest in share of a company shall make a declaration to the company specifying the nature of his interest, particulars of the person in whose name the shares stand registered in the books of the company and such other particulars as may be prescribed.

(3) Where any change occurs in the beneficial interest in such shares, the person referred to in sub-section (1) and the beneficial owner specified in sub-section (2) shall, within a period of thirty days from the date of such change, make a declaration to the company in such form and containing such particulars as may be prescribed.

(4) The Central Government may make rules to provide for the manner of holding and disclosing beneficial interest and beneficial ownership under this section.

(5) If any person fails, to make a declaration as required under sub-section (1) or sub-section (2) or sub-section (3), without any reasonable cause, he shall be punishable with fine which may extend to fifty thousand rupees and where the failure is a continuing one, with a further fine which may extend to one thousand rupees for every day after the first during which the failure continues.

(6) Where any declaration under this section is made to a company, the company shall make a note of such declaration in the register concerned and shall file, within thirty days from the date of receipt of declaration by it, a return in the prescribed form with the Registrar in respect of such declaration with such fees or additional fees as may be prescribed, [xxx]

(7) If a company, required to file a return under sub-section (6), fails to do so before the expiry of the time specified [therein], the company and every officer of the company who is in default shall be punishable with fine which shall not be less than five hundred rupees but which may extend to one thousand rupees and where the failure is a continuing one, with a further fine which may extend to one thousand rupees for every day after the first during which the failure continues.

(8) No right in relation to any share in respect of which a declaration is required to be made under this section but not made by the beneficial owner, shall be enforceable by him or by any person claiming through him.

(9) Nothing in this section shall be deemed to prejudice the obligation of a company to pay dividend to its members under this Act and the said obligation shall, on such payment, stand discharged.

(10) For the purposes of this section and section 90, beneficial interest in a share includes, directly or indirectly, through any contract, arrangement or otherwise, the right or entitlement of a person alone or together with any other person to—

(i) exercise or cause to be exercised any or all of the rights attached to such share; or

(ii) receive or participate in any dividend or other distribution in respect of such share

Sometimes a person, known as benamidar, may hold some shares for the benefit of another person known as the beneficial owner. Although the latter has the beneficial interest in the shares, the former stands registered as shareholder in the books of the company. Section 89 makes it obligatory for both the benamidar as well as the beneficial owner of the shares to make a declaration to that effect. Such declaration is required to be made within 30 days from the enforcement date of the Companies (Amendment) Act, 1974 or within 30 days after his becoming such beneficial owner.

If any change takes place in the beneficial interest in such shares, the beneficial owner is required to make a declaration to the company within 30 days from the date of such change.

Where such a declaration is made to the company, the company is required to make a note of such declaration in its register of members and to file a return in the prescribed form to the Registrar with regard to such declaration within 30 days from the date of the receipt of the declaration.

To make the provision more effective, several kinds of penalties have been provided in case of default. Every person who fails, without any reasonable cause, to make a declaration is punishable with a fine which may extend to rupees fifty thousand and a further fine of rupees one thousand per day during which the default continues. If a company fails to comply, the company, and every officer of the company in default is punishable with fine which may extend to Rs.100/- for everyday during which the default continues. Besides, if declaration is not made in accordance with the provisions of this section, any charge, promissory note or any other collateral agreement, created, executed or entered into in relation to any share by the ostensible owner thereof or any hypothecation by the ostensible owner in respect of the shares shall not be enforceable by the beneficial owner or any person claiming through him. The Central Government, as Sec.90 provides, may appoint one or more

inspectors to investigate and report as to whether the provisions of Sec.89 have been complied with, with regard to any share and after such appointment the provisions of Sec.216 shall apply to such investigation.

5. Terminator or Cessation of Membership

Cessation of Membership means, "termination of membership". A person ceases to be a member or loses membership in the following two ways, namely:

1. Act of the parties; or
2. Operation of law.

1. Cessation of membership by act of the parties: A person may cease to be the member of a company –

1. If he transfers his shares to another person.
2. If his shares are forfeited.
3. If the company sells his shares under some provision in its Articles (E.g.: to enforce a lien).
4. If he rescinds the contract to take shares on the ground of misrepresentation in the prospectus or on the ground of irregular allotment.
5. If redeemable preference shares are redeemed.
6. If he surrenders his shares, where surrender is permitted.
7. If share warrants are issued to him in exchange of fully paid shares.

2. Cessation of membership by operation of law: This covers the following cases:

1. *Insolvency:* The shares of an insolvent vest in the Official Receiver or Assignee. When the Official Receiver or Assignee transfers his shares to another person, the insolvent ceases to be a member on the registration of the transferee as a member. But the insolvent remains a member as long as his name is not removed from the register of the company [*Wise vs. Lansdell* (1921) 1Ch. 420 (Ch.D.)].

2. *Death:* The deceased member's estate, however, remains liable until the shares are registered in the name of his legal representative.

3. Sale of shares in execution of a decree of a Court.

4. *Winding up of the Company:* However, during the winding up of a company a member continues to be liable as a contributory and is also entitled to share in the surplus assets, if any.

6. Rights and Liabilities of Members or Shareholders

Rights of Members or Shareholders: Rights of the shareholders may be divided into the following categories:

1. individual Rights (or individual Membership Rights).
2. rights of the minority shareholders.
3. rights of the majority shareholders (or Corporate Membership Rights).

Individual Rights or Individual Membership Rights: Shareholders are given certain rights in their individual capacity. A shareholder is entitled to enforce his individual rights in his own name. In other words, if a shareholder complains of an unlawful infringement of a right qualifying as an individual membership right, he can sue in his own name and this right of action will not be affected by any decision of the majority.

The individual rights of a shareholder include the right –

i. To maintain (himself) in full membership with all the rights and privilege appertaining to that status. This right implies that the individual shareholder can insist on the strict observance of the legal rules, statutory provisions and provisions in memorandum and articles, which cannot be waived by a bare majority of shareholders.

ii. Of not being compelled to subscribe for more shares.

iii. To compel the company not to increase his liability without his consent.

iv. To inspect the register of members and debentureholders, annual returns, register of investment, contracts, directors' shareholdings, loans to companies under the same management and the minute books of general meeting and also to obtain copies thereof after paying the prescribed fees.

v. To transfer his shares subject to restrictions (if any) imposed by the articles of the company.

vi. To receive information of the allotment of the shares in his favour.

vii. To have his name entered in the company's register of members and to have the register rectified. If the company refuses to rectify the register, he can apply to the person or proxy.

viii. To receive notice of the meetings of the company, to attend them and to vote at them either in person or proxy.

ix. To receive notice of any resolution requiring special notice.

x. To apply to the Central Government for calling an annual general meeting of the company, if the company defaults in the holding of such meetings.

xi. To receive a copy of statutory report, except in the case of private company.

xii. Of pre-emption.

xiii. To receive dividends, when declared and in case the dividends are paid on ultra vires declaration or out of capital, to apply to the Tribunal for an injunction to prevent the directors to do so.

xiv. To obtain a copy of the balance sheet, profit and loss account and the auditor's report.

xv. To take part in the appointment of the company's auditors at its annual general meeting and to inspect the report of auditors at its annual general meeting.

xvi. To object to the appointment of two or more directors by a single resolution but this right is available only in case of a public company.

xvii. To petition for a compulsory winding up of the company.

xviii. On dissolution of the company, if any surplus assets are found, to receive a share therein.

Liabilities of Members: The liability of the members of a company depends on the nature of the company.

Company with unlimited liability. Each member is liable in full for all the debts contracted by the company during the period he was a member.

Company limited by shares. Each member is liable to pay the full nominal value of the shares held by him. If he has already paid a part of the amount on the shares, his liability is limited to the unpaid amount on the shares in respect of which he is a member.

The liability of a registered shareholder to pay for the shares standing in his name arises from the operation of Sec.10 (Corresponding to Section 36 of the Companies Act, 1956), which provides that all moneys payable by any member to the company under the Memorandum or the Articles are a debt due from him to the company. Further, it is the registered holder of shares, whether he is a beneficial owner of a mere trustee, who is liable to pay the amounts due on shares.

Where a shareholder dies, his estate is liable in respect of his partly paid shares, and when these shares are registered in the name of his legal representatives, they become liable on those shares. Where he is adjudicated insolvent, the Official Receiver or Assignee may either sell the partly paid shares in which case the buyer would become liable in respect thereof or he may disclaim them as onerous property.

If at any time the number of members is reduced below 7 (2) in the case of a private company), and the company carries on business for more than 6 months while the number is so reduced, every member who knows that the number is so reduced becomes severally liable for the payment of the whole of the debts of the company.

Company limited by guarantee. Each member is liable to contribute the amount guaranteed by him to be paid in the event of the winding up of the company.

Lecture–X
DEBENTURES AND CHARGES

This lecture covers —

1. Debenture: Meaning, Definition, Nature and Kinds.
2. Debenture Trust Deed (Secs.117.A – 117.C).
3. Creation of Charges (or charges securing debentures or Fixed and Floating Charges).

1. Debenture: Meaning, Definition, Nature and Kinds

Meaning: The most usual process of borrowing by a company limited by shares is by the issue of shares. The shareholder invests money (capital) in a company in consideration of dividend, while the debenture holder lends money to the company in return for interest.

'Debenture' means a document which either creates a debt or acknowledges it [*Levy v. Abercorris Slate & Slab Co.* (1887) 37 Ch.D. 260].

In *Edmonds v. Blaina Co.* (1887) 36 Ch.D. 215, Chitty J. described the meaning of the term 'debenture' as follows:

"The term itself imports a debt – an acknowledgement of a debt – and obligation or covenant to pay. This obligation or covenant is in most cases accompanies by some charge or security".

Debenture is a certificate issued by a company indicating the debt owed by the company to the holder thereof. Debenture certificate indicates the debt owed by the company to a debenture holder against the loan taken by the company.

Debenture certificate bears a distinctive number and is one of the series of the documents, indicating the amount of debt and the interest payable thereon, charging all the property of the company, whether present or future, for the payment of the same.

Debentures are commonly issued in a manner similar to the issue of shares through a prospectus. The amount might be payable

by installments on application, allotment and calls. But usually the amount is payable in one lump sum.

Definition: No satisfactory definition of this term is found in English or Indian Companies Act. Sec.455 of the English Companies Act provides that 'debenture includes debenture stock, bonds and any other securities of a company whether consisting a charge on the assets of the company or not.' This definition has been adopted in Sec.2(12) of the Indian Companies Act 1956.

Palmer defines – 'an instrument under seal evidencing a debt, the essence of its being the admission of indebtedness.'

According to Topham: 'Debenture is a document given by a company as evidence of a debt to the holder usually arising out of a loan and most commonly secured by charge'.

In *Laxman Bharamji v. Emperor* (AIR 1946 Bom. 18), a company issued certain document for money, the documents bore serial numbers, acknowledged a debt and provided for paydment of interest by determining lucky number, the court held them to be debentures despite the fact that they were described as patron bonds. Thus, to determine whether a particular document issued by a company is debenture or not, the court looks at the substance of the transaction.

In *Levy v. Abercorris State & Co.* (1887) 37 Ch. D 260, 264) Chitty J. defined thus: 'Debenture' means a document which either creates a debt or acknowledges it, and any docudment which fulfils either of these conditions is a debenture.

In *Lemon v. Austrian Friar's Trust* (1926) Ch. 1, the term 'debenture' was explained by the Court of Appeal as "something which was a mere acknowledgement of indebtedness, without containing a charge at all."

According to Section 2(12), 'debenture' includes debenture stock, bonds and any other securities of a company, whether constituting a charge on the assets of the company or not. Section 2(12), however, does not explain as to what a debenture really is.

According to Section 2(30) of the Companies Act, 2013, 'debenture' includes debenture stock, bonds or any other instrument

of a company evidencing a debt, whether constituting a charge on the assets of the company or not.

Provided that, -

(a) The instrument referred to in Chapter III-D of the Reserve Bank of India, 1934; and

(b) Such other instrument, as may be prescribed by the Central Government of India in consultation with Reserve Bank of India, issued by a Company,

shall not be treated as Debenture.

If a company finds difficult to meet all financial requirements with the help of the capital raised by issue of shares, it resorts to borrow large sums of money by issuing debentures.

Features or Characteristics of Debenture: In order to discuss the characteristic features of a debenture, the following definition of debenture given in *Lemon vs. Austin Friars Investment Trust Ltd.* (1926) Ch. 1 (C.A) may be noted:

"A debenture is a document containing an acknowledgement of indebtedness which need not be, although it usually is, under seal, which need not give, although it usually does give, a charge on the assets of the company, by way of security, and which may or may not be one of a series".

In the light of this definition, the characteristic features of a debenture are as follows:

1. It is issued by a company and is usually in the form of a certificate, which is an acknowledgement of indebtedness.
2. It is issued under the company's seal. It need not, however, be necessarily under the company's seal.
3. It is one of a series issued to a number of lenders. But a single debenture is also not uncommon. Thus a mortgage of a company property to a single individual as security for a loan is a debenture within the definitions given earlier.
4. It usually specifies a particular period or date as the date of repayment. It also provides for the payment of a specified principal and interest at the specified date. But a company is not debarred from issuing perpetual or irredeemable debentures.
5. It generally creates a charge on the undertaking of the company or some parts of its property; but there may be debentures without any such charge.

6. A debenture-holder does not have any right to vote in the company meetings.

Contents of Debentures: A debenture usually contains four main clauses, namely –

i) A promise by the company to repay the principal amount on a certain fixed date.

ii) A promise to pay interest at a fixed rate.

iii) A charge on the company's assets, and

iv) A provision that debenture is issued subject to conditions which are endorsed on it.

Nature of debenture (Sec.44): Section 44 (Corresponding to Section 82 as amended by the Companies (Amendment) Act, 1999] deals with the nature of shares and debentures. The debentures of a company are a movable property, transferable in the manner provided by the Articles.

Distinction between Debenture and Share or Debenture-holder and Shareholder: Following are the notable points of distinction between the debenture-holder and shareholder.

1. A debenture-holder is a creditor of the company, whereas a shareholder is its member.
2. A debenture-holder does not have a right to vote at any meeting of the company, whereas a shareholder has a voting right.
3. A debenture-holder is entitled to a fixed rate of interest on his investment, whereas a shareholder gets dividend out of profits. In case of equity shares the rate of dividend depends on the amount of profits. In case of preference shares, however, fixed rate of dividend may be payable.
4. Shares (except preference shares) cannot be paid back, or redeemed. Debentures can be redeemed.
5. Debenture holders being the creditors of the company, when the company is wound up they get priority in payment over the shareholders of the company.

Register and Index of debenture holders (Sec.88): Section 88 of Companies Act, 2013 (Corresponding to Section 152 of the Companies Act, 1956) envisages the maintenance of the Register and Index of Debenture holders. According to Section 88, every company issuing debentures is required to maintain a register of debenture holders in which it is to enter

i. the name, address, and the occupation (if any) of the debenture holder;

ii. the number of debentures held by each holder and the amount paid, or agreed to by paid in respect thereof;

iii. the date at which each person was entered in the register as a debenture holder; and

iv. the date at which any person ceased to be a debenture holder.

Every company having more than 50 debenture holders shall, unless the register of debenture holders is in such a form as in itself to constitute an index, keep an index of all the debenture holders.

Kinds of Debentures: There are various kinds of debentures. Notable among them are stated below:

1. Bearer Debentures and Registered Debentures.
2. Redeemable Debentures and Irredeemable or Perpetual Debentures.
3. Unsecured or Naked Debentures and Secured or Mortgage Debentures.
4. Convertible and Non-convertible Debentures.

1. Bearer Debentures and Registered Debentures: According to Sec.88, every company is required to keep a register of debenture holders, which is to contain various particulars including the name, address and occupation of each debenture holder. When the name of the debenture-holder is mentioned on the debenture certificate and is recorded in the debenture holders register, he is a registered debenture holder. He may transfer such debentures just like shares, by executing the instrument of transfer. Such debentures

are called 'registered debentures'. The transfer of registered debenture is required to be registered with the company.

Sometimes the debentures may be payable to bearer. Such debentures could be transferred like bearer negotiable instrument, by mere delivery. A bearer debenture is like a negotiable instrument transferable by mere delivery and also constituting the transferee as a holder in due course. Moreover, the holder of the bearer debenture may be presumed to be a holder in due course, under Sec.118 of the Negotiable Instruments Act, 1881.

2. Redeemable Debentures and Irredeemable or Perpetual Debentures: When a company issues debentures it specifies the period of the loan, or in other words, it mentions the terms on the expiry of which they are to be redeemed. The company is to redeem such debentures on the expiry of the requisite period. The company redeeming the debentures can re-issue the same, and when the same are re-issued, the person now entitled to the debentures shall have the rights and priorities as if the debentures had never been redeemed.

A Company can issue such debentures also which the company may not redeem or buy back. Such debentures are known as irredeemable or perpetual debentures. A Company has also the power to issue debentures the redemption of which is unusually long, or the redemption of which depends only on happening of a remote contingency. A condition in the debentures that they shall be irredeemable or redeemable only on the happening of a contingency, however remote, or on the expiration of a period however long, shall not be considered to be invalid.

3. Unsecured or Naked Debentures and Mortgage Debentures: An unsecured debenture is called naked debenture. Such debentures do not carry any charge on the property of the company. Thus, they are not given any security as to the payment of principal money and interest due thereon. They contain only a promise to pay and nothing more.

Mortgage debentures are those which are secured by a charge on the whole or part of the property of the company. Such debentures are used for long-term borrowing.

4. Convertible and Non-convertible Debentures: Convertible debentures are those debentures which give an option to the holders to convert them into preference or equity shares at stated rates of exchange, after a certain period. If the holders exercise the right of conversion, they cease to be lenders to the company and become members instead. The convertible debentures may be fully convertible (FCD) or partly convertible (PCD).

Non-convertible debentures are those debentures, which do not give any option to their holders to convert them into preference or equity shares. They are to be duly paid as and when they mature.

Distribution between shares and Debentures: Share holder is a investor in a public company (company limited by shares) while debenture holder is creditor of the company. Following are the notable points of difference between the share-holder and debenture-holder.

Share-holder	Debenture-holder
1. The share holders have the right of control and interference in the company's affairs.	1. The debenture holders have no control in the company's affairs.
2. The share holders are entitled to get dividends only out of profit.	2. The debenture holders are entitled to a fixed rate of interest, whether the company runs on profit or loss.
3. The share holders cannot be paid up as long as company is a going concern.	3. Except in case of perpetual debenture holders, the company can pay back the other debenture holders.
4. The share holders are paid back only after all other claims have been paid.	4. Ordinarily, a debenture holder being a secured creditor, in winding up, is paid as a priority.

2. Debenture Trust Deed

Section 71(7) of the Companies Act, 2013 (Corresponding Sections 117.A to 117.C of the Companies Act, 1956 as inserted by the Companies (Amendment) Act, 2000)provides for securing any issue of debentures, which shall be open for inspection to any member or debenture holder of the company. The member or debenture holder is entitled to get a copy of the debenture trust deed on payment of a prescribed fee. Sub section (10) provides that in case failure to comply with the above provision, the company shall be liable to pay interest on the debenture when it is due and the Tribunal after hearing the parties, may order the Company to pay principal with interest.

Debenture Trustees: Section 71(5) provides for the appointment of debenture trustees and enumerates the duties of such trustees. It provides that no company shall issue a prospectus or a letter of offer to the public for subscription of its debentures, unless the company has, before such issue, appointed one or more debenture trustees for such debentures and the trustees have given their consent to the company to be so appointed.

Liability of Company to create security and Debenture Redemption Reserve: Where a company issues debentures after the commencement of this Act, it shall create a debenture redemption reserve for the redemption of such debentures, to which adequate amounts shall be credited, from out of its profits every year until such debentures are redeemed.

Where the company fails to redeem the debentures on the date of maturity, the Tribunal may, on the application of any or all the debenture holders, after hearing the parties concerned, direct the company to redeem the debentures forthwith along with interest due thereon.

If default is made in complying with the order of the Tribunal, the officer of the company who is in default shall be punishable with imprisonment which may extend to three years and shall also be liable to a fine of not less than two lakh rupees which may extend to five lakh rupees, or with both.

Re-issue of Redeemed Debentures: A company which has redeemed some of the debentures of a series the redeemed debentures unless –

a) The articles or the conditions of issue provide otherwise, or

b) The company is under a contract not to re-issue the redeemed debentures, or

c) The company has, by resolution or otherwise manifested an intention to cancel the redeemed debentures.

The object of this section is to override the principle according to which a debenture once paid off was extinguished, and could not be reissued.

When a company has power to reissue debentures which have been redeemed, particulars of the redeemed debentures which can be reissued must be stated in every balance sheet.

The holders of reissued debentures have the same rights and priorities as if the debentures; had never been redeemed, i.e. they *rank paripassu* with the debentures left unredeemed. A company cannot reissue redeemed debentures containing provisions as to redemption different from those of the original issue.

A reissued debenture requires the same stamp as a new debenture, but failure to re-stamp does not affect the holder if he was unaware of the default.

Debentures deposited to secure advances on current account or otherwise are not deemed to have been redeemed only by reason of the account having ceased to be in debit. Thus where such an account is temporarily in credit and again in debit, the debentures deposited as security are not deemed to have been redeemed and reissued so as to require re-stamping.

Debenture-holders of a company, who are usually in large numbers, may not have the time to look after their interest in the property mortgaged or charged. They may, in order to protect and safeguard their interest, appoint some persons (usually some from among them) as trustees. A trust deed is in such a case executed,

conveying the property of the company to trustees. Under the terms of the trust deed the company undertakes to pay to the debenture-holders their principal and interest, and normally charges its property to the trustees as security.

The trustees must act diligently and honestly in the discharge of their duties. Any clause in the trust deed which exempts them from liability for breach of their duty as trustees is void.

The trust deed contains the terms and conditions endorsed on the debentures and defines the rights of debenture-holders and the company. It usually empowers the trustees to appoint a receiver to protect their interest. It also contains other provisions concerning meetings of the debenture-holders, supervision of the assets charged, and the keeping of a register of debenture-holders.

Whenever there is default by the company action may be taken by the trustees on behalf of all the debenture-holders.

3. Creation of Charges (or Charges Securing Debentures or Fixed and Floating Charges)

Charge: The word 'Charge' signifies security for payment of a debt or performance of an obligation. For the purpose of this chapter, charge includes a mortgage. Charge may be defined as a security given for securing loans or debentures by a mortgage on the assets of a company. Generally, the debentures and other securities of a company are secured by a charge on its assets. A charge is created, when a property, whether existing or future, is agreed to be made available as a security for the repayment of a debt.

The debt owed by a person (debtor) to another (creditor) may be either unsecured or secured. In the former case, if the debtor defaults, the creditor can sue for the amount owed i.e. he has a right of action. If the debtor becomes insolvent or disappears, the creditor has no security. A wise creditor, therefore, will demand security, i.e. a right over the debtor's property, which is in addition to his right of action. A bank overdraft, for instance, is often secured by a deposit of the title deeds of the borrower's house (a mortgage), or of his

share certificates (a pledge). A Company like any other person can, when it borrows money, give its creditors security. Often it mortgages or charges its property to its debenture-holders. However, the creditor gets no legal right over the property so charged, but only gets a right to have the security made available by the order of the court in the event of non-payment of a debt.

According to Section 2(16) of the Companies Act, 2013 a charge means an interest or lien created on the property or assets of a company or any of its undertakings or both, as security and includes a mortgage.

A Company can issue debentures either unsecured or secured by a charge on its property. Kinds of charge: A charge on the property of a company as security for debentures or debt is classified into two heads, namely —

1. Fixed charge or specific charge.
2. Floating charge.

1. Fixed or Specific Charge: It means a charge on definite and ascertained property. When debentures are secured by a certain charge on definite and ascertained property of the company like land or ships, etc. it is said that the debentures have been secured by a fixed or specific charge. Thus, under a fixed charge certain property of the company is mortgaged with the holder of debentures and the company cannot transfer the property under charge without the consent of the holder of charge and if it is transferred without his consent, the transfer will be effective subject to the charge.

Thus, after the creation of a fixed charge on a property, the company cannot deal with the property charged so as to effect the right of the holder of the charge. In the winding up of the company the holder of a debenture secured by a fixed charge ranks as a secured creditor in respect of the debt due to him on the debenture. The secured creditor, in the case of a fixed charge, gets priority in repayment over the other creditors. When some specific property is subject to a charge, the same cannot be disposed of or dealt with by the company as an unencumbered property.

2. Floating Charge: A floating charge is not a charge of any specific asset or assets. It is a charge on a class of assets both present and future. A floating charge is an equitable charge, which is created on some class of property, which is constantly changing, E.g.: a charge on stock-in-trade, trade debtors, etc. It means all the property, present or future, of the company, since it is an unstable property, a charge created thereon will be floating. The main idea behind a floating charge is to allow the company to carry on its business in the ordinary course as if no charge had been created.

Section 332 of the Companies Act, 2013 provides that a floating charge created by a company in winding up on the basis of business property and assets held by it one year prior to date of its winding up shall not be valid until it is proved that the company's financial condition was sound at the time such charge was created.

Government Stock Company vs. Manilal Rail Co. (1897) AC 81 – In this case, Lord Macnaghten has explained the nature of a floating charge in the following words:

"A floating security is an equitable charge on the assets for the time being of a going concern."

It attaches to the subjects changed in varying conditions in which it happens to be from time to time. It is of the essence of such a charge that it remains dormant until the undertaking charge ceases to be a going concern, or until the person in whose favour the charge is created intervenes.

Crystallisation of Floating Charge: A floating charge generally remains dormant until it crystallizes or becomes a fixed charge. A floating charge crystallizes into a fixed security under the following circumstances.

i) When company goes into liquidation.

ii) When company ceases to carry on business.

iii) When debenture holders or creditors take steps to enforce this security E.g: by appointing a receiver to take possession of the charged property.

iv) On happening of an event specified in the deed.

Until a floating charge crystallizes into a fixed one, the company can deal with the property so charged in any manner it likes.

In *Maturi U. Rao v. Pendyala* (AIR (1970) AP 225), the High Court of Andhra Pradesh held that the essence of floating charge is that the security remains dormant until it is fixed or crystallizes.

Characteristics: The chief characteristics of a floating charge have been summed up by Justice Romer in Re, Yorkshire Woolcombers' Association, [(1903) 2 Ch. 284]. His Lordship said that mortgage or charge will be treated as a floating charge, if–

1. it is a charge upon a class of assets both present and future;
2. the class of assets upon which the charge has been created must be one which in the ordinary course of the business of the company would be changing from time to time; and
3. it has been contemplated by the charge that until some step is taken by the mortgagee, the company can use the assets comprised in the charge in the ordinary course of business.

In *Re Indus Film Corporation Ltd.* (AIR 1939 Sindh 100), a film company borrowed a sum of money and declared a lien on all its assets including machinery etc. which was then lying or might be brought thereafter until repayment. This was held to be a floating charge as it covered assets present and future, of extremely fluctuating type and imposed no restriction on them.

In *Re Hi Fi Equipment (Cabines) Ltd.* (1988) BCLC 65 Ch.D), a charge was created on 'fixed plant and machinery' which would have been a fixed charge, but since the company had no firmly fixed machinery, it was held to be a floating charge.

In *State of A.P v. Sri Raja Ram Janardhana* (1965) 2 Comp. LJ 222) – the Andhra Pradesh High Court observed that where the debentures are secured solely by a floating charge, the company may dispose of the property on which the charge exists unencumbered without consulting the holders of the charge i.e. debenture holders in this case, until an event happens (winding up in

this case) on which the floating charge crystallizes i.e. becomes a fixed charge. Before crystallization, the company is free to dispose of the property charged I ordinary course of its business.

Effects of Floating Charge (Sec.332): A floating charge gets priority over the unsecured creditors of the company, whether there is winding up or not. Section 332, however, provides that a floating charge which has been created within 12 months immediately preceding the commencement of winding up shall be invalid, except in the following cases:

1. When it is proved that immediately after the creation of the charge the company was solvent. It means that if the company was solvent immediately after the creation of the charge, the charge would be valid inspite of its having been created within 12 months immediately preceding the commencement of winding up.
2. If any cash has been paid to the company under the charge, the charge would be valid in respect of such amount and interest thereon @ 5% p.a. or such other rate as may be notified by the Central Government.

Distinction between Fixed and Floating Charge: Following are the notable points of distinction between Fixed and Floating charge.

1. Fixed charge is created on a definite and ascertained property of the company while floating charge is created on the properties, which are unstable or changing in their nature.
2. Until a floating charge becomes fixed or cystallised, the company can deal with the property under charge in the ordinary course of business in any way authorised by its memorandum or articles. In other words, the company can sell, mortgage, exchange or lease the property charged in the ordinary course of its business, if it is so authorised by its memorandum or articles, and their right of the company will continue so long as the floating charge does not come fixed or crystallised. But in the case of a floating charge the company

cannot deal with the property under charge so as to effect the rights of the holder of the charge.

3. Assets subject to a floating charge may in the ordinary course of business charge from time to time but assets under a fixed charge cannot be charged except with the consent of the holder of the charge.

4. There are certain claims which have priority over the claim of the holder of a floating charge but nobody is allowed to have priority over the holder of a fixed charge in respect of the property subject to such charge.

Lecture – XI

COMPANY DIRECTORS (POSITION, POWERS AND DUTIES)

This lecture covers the following heads:

1. Director: Meaning and Definition.
2. Qualification.
3. Appointment of Director (Section 152).
4. Disqualifications of Directors (Sec.164).
5. Kinds of Directors.
6. Position of Directors.
7. Powers of Directors (Sec.179).
8. Duties and Liabilities of Directors.
9. Vacation of Office by Director (Sec.167).
10. Resignation by a Director (Sec.169).
11. Removal of Directors (Sec.169).

Chapter XI containing Sections 149 to 172 of the Companies Act, 2013 lays down the provisions relating to qualifications, appointment, duties etc. of the Board of Directors. Section 149 envisages a company to have a Board of Directors. Section 150 prescribes manner of selection of independent directors and maintenance of databank of independent directors. Section 151 provides for appointment of Director elected by small shareholders. Section 152 deals with the appointment of Directors. Section 153 prescribes application for allotment of Director Identification Number. Section 154 prescribes allotment of Director Identification Number. Section 155 prohibits obtaining more than one Director Identification Number. Section 156 imposes an obligation on Director to intimate Director Identification Number. Section 157 envisages company to inform Director Identification Number to Registrar. Section 158 while furnishing returns any return, imposes an obligation to indicate Director Identification Number. Section 159 prescribes punishment

for contravention of the provisions under Sections 152, 155 and 156. Section 160 provides for Right to persons other than retiring directors to stand for directorship. Section 161 makes provisions for appointment of additional director, alternate director and nominee director. Section 162 deals with appointment of directors to be voted individually. Section 163 deals with option to adopt principle of proportional representation for appointment of directors. Section 164 prescribes disqualifications for appointment of director. Section 165 prescribes number of directorships. Section 166 lays down the provisions relating to duties of directors. Section 167 provides for vacation of office of director. Section 168 prescribes procedure for resignation of director. Section 169 lays down the procedure for removal of directors. Section 170 deals with register of directors and key managerial personnel and their shareholdings. Section 171 confers on members' right to inspect and Section 172 prescribes punishment for contravention of the provisions of this Chapter XI.

1. Director: Meaning and Definition

Company is an artificial person created by law with perpetual existence and common seal. A company being an artificial person, it cannot have body or mind to act independently. It can act only through human agents, who are called 'Directors'.

'The company itself cannot act in its own person, for it has no person; it can only act through directors, and the case is, as regards those directors, merely the ordinary case of principal and agent.'

Lord Cranworth L.C. observedin ***Aberdeen Rly. Co. v. Blaikie Bros.*** **(1854) 1Macq. 461** – 'The directors are a body to whom is delegated the duty of managing the general affairs of the company. A corporate body can only act by agents, and it is of course the duty of those agents so to act as best to promote the interests of the corporation whose affairs they are conducting.'

Directors or Board of Directors play an important role in the administration and Management of the Company. The success of the company and the welfare of the shareholders depend on the efficient administration of the Directors. Since, the directors are the brains of the Company.

According to Section 149 of the Companies Act, 2013 (Corresponding to Section253 of the Indian Companies Act, 1956), only individuals can be appointed as Directors. Section 149 says, 'No body corporate, association or firm shall be appointed director of a company, and only an individual shall be appointed'. Section 149 reads as follows–

Company to have Board of Directors— (1) Every company shall have a Board of Directors consisting of individuals as directors and shall have:

(a) a minimum number of three directors in the case of a public company, two directors in the case of a private company, and one director in the case of a One PersonCompany; and

(b) a maximum of fifteen directors: Provided that a company may appoint more than fifteen directors after passing a special resolution: Provided further that such class or classes of companies as may be prescribed, shall have at least one woman director.

(2) Every company existing on or before the date of commencement of this Act shall within one year from such commencement comply with the requirements of the provisions of sub-section (1).

[(3) Every company shall have at least one director who stays in India for a total period of not less than one hundred and eighty-two days during the financial year:

Provided that in case of a newly incorporated company the requirement under this sub-section shall apply proportionately at the end of the financial year in which it is incorporated.]

(4) Every listed public company shall have at least one-third of the total number of directors as independent directors and the Central Government may prescribe the minimum number of independent directors in case of any class or classes of public companies.

Explanation: For the purposes of this sub-section, any fraction contained in such one-third number shall be rounded off as one.

(5) Every company existing on or before the date of commencement of this Act shall, within one year from such commencement or from the date of notification of the rules in this regard as may be applicable, comply with the requirements of the provisions of sub-section (4).

(6) An independent director in relation to a company, means a director other than a managing director or a whole-time director or a nominee director:

(a) who, in the opinion of the Board, is a person of integrity and possesses relevant expertise and experience;

(b) (i) who is or was not a promoter of the company or its holding, subsidiary or associate company;

(ii) who is not related to promoters or directors in the company, its holding, subsidiary or associate company;

(c) who has or had no [pecuniary relationship, other than remuneration as such director or having transaction not exceeding ten per cent. of his total income or such amount as may be prescribed] relationship with the company, its holding, subsidiary or associate company, or their promoters, or directors, during the two immediately preceding financial years or during the current financial year;

[(d) none of whose relatives—

(i) is holding any security of or interest in the company, its holding, subsidiary or associate company during the two immediately preceding financial years or during the current financial year:

Provided that the relative may hold security or interest in the company of face value not exceeding fifty lakh rupees or two per cent. of the paid-up capital of the company, its holding, subsidiary or associate company or such higher sum as may be prescribed;

(ii) is indebted to the company, its holding, subsidiary or associate company or their promoters, or directors, in excess of such amount as may be prescribed during the two immediately preceding financial years or during the current financial year;

(iii) has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, its holding, subsidiary or associate company or their promoters, or directors of such holding company, for such amount as may be prescribed during the two immediately preceding financial years or during the current financial year; or

(iv) has any other pecuniary transaction or relationship with the company, or its subsidiary, or its holding or associate company amounting to two per cent. or more of its gross turnover or total income singly or in combination with the transactions referred to in sub-clause (i), (ii) or (iii);]

(e) who, neither himself nor any of his relatives:

(i) holds or has held the position of a key managerial personnel or is or has been employee of the company or its holding, subsidiary or associate company in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed;

[Provided that in case of a relative who is an employee, the restriction under this clause shall not apply for his employment during preceding three financial years.]

(ii) is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed, of:

(A) a firm of auditors or company secretaries in practice or cost auditors of the company or its holding, subsidiary or associate company; or

(B) any legal or a consulting firm that has or had any transaction with the company, its holding, subsidiary or associate company amounting to ten per cent. or more of the gross turnover of such firm;

(iii) holds together with his relatives two per cent. or more of the total voting power of the company; or

(iv) is a Chief Executive or director, by whatever name called, of any non-profit organisation that receives twenty-five per cent. or more of its receipts from the company, any of its promoters, directors or its holding, subsidiary or associate company or that holds two per cent. or more of the total voting power of the company; or

(f) who possesses such other qualifications as may be prescribed.

(7) Every independent director shall at the first meeting of the Board in which he participates as a director and thereafter at the first meeting of the Board in every financial year or whenever there is any change in the circumstances which may affect his status as an independent director, give a declaration that he meets the criteria of independence as provided in sub-section (6).

Explanation: For the purposes of this section, "nominee director" means a director nominated by any financial institution in pursuance of the provisions of any law for the time being in force, or of any agreement, or appointed by any Government, or any other person to represent its interests.

(8) The company and independent directors shall abide by the provisions specified in Schedule IV.

(9) Notwithstanding anything contained in any other provision of this Act, but subject to the provisions of sections 197 and 198, an independent director shall not be entitled to any stock option and may receive remuneration by way of fee provided under sub-section (5) of section 197, reimbursement of expenses for participation in the Board and other meetings and profit related commission as may be approved by the members.

(10) Subject to the provisions of section 152, an independent director shall hold office for a term up to five consecutive years on the Board of a company, but shall be eligible for re-appointment on passing of a special resolution by the company and disclosure of such appointment in the Board's report.

(11) Notwithstanding anything contained in sub-section (10), no independent director shall hold office for more than two consecutive terms, but such independent director shall be eligible for appointment after the expiration of three years of ceasing to become an independent director:

Provided that an independent director shall not, during the said period of three years, be appointed in or be associated with the company in any other capacity, either directly or indirectly.

Explanation: For the purposes of sub-sections (10) and (11), any tenure of an independent director on the date of commencement of this Act shall not be counted as a term under those sub-sections.

(12) Notwithstanding anything contained in this Act,—

(i) an independent director;

(ii) a non-executive director not being promoter or key managerial personnel,

shall be held liable, only in respect of such acts of omission or commission by a company which had occurred with his knowledge, attributable through Board processes, and with his consent or connivance or where he had not acted diligently.

(13) The provisions of sub-sections (6) and (7) of section 152 in respect of retirement of directors by rotation shall not be applicable to appointment of independent directors.

Number of Directors: According to Section 149 of the Companies Act, —

a) every public limited company must have atleast three directors, and every private company must have at least two directors. Articles of Association of the company provides for the appointment of Directors, and every one person company must have one director, and

b) a maximum number of 15 directors. However, a company by passing a special resolution appoint more than 15 directors.

Articles of Association of the Company provides for the appointment of Directors.

Woman Director: According to Rule 3 of the Companies (Appointment and Qualification of Directors) Rules, 2014, the following class/classes of companies shall have at least one Women Director.

1) Every listed company.
2) Every other public company having
   a) Paid up share capital of one hundred crore rupees or more, or
   b) Turnover of three hundred crore rupees or more as on the last date of the latest audited financial statement.

Definition: Section 2(34) of the Companies Act, 2013, 'director' means "a director appointed to the Board of a Company" (The corresponding Section 2(13) of the Companies Act, 1956) defines director as 'director' includes any person occupying the position of director, by whatever name called.

Bowen L.J. defines – 'Directors are described sometimes as agents, sometimes, as trustees and sometimes as managing partners. But each of these expressions is used not as exhaustive of their powers and responsibilities, but as indicating useful points of view from which they may for the moment and for the particular purpose be considered.'

Lord Selborne L.C. defines – 'The directors are the mere trustees or agents of the company – trustees of the company's money

and property – agents of the transactions which they enter into on behalf of the company.'

***Lord Johnston** defines* – 'The director's functions are in one view those of an agent, and in another those of trustee. But the former predominate over the latter.'

***Lush L.J.** defines* – 'A director is not a servant of any master. He cannot be described as a servant of the company or of any one'.

***Mccardie J.** defines* – 'A director is in fact a director or controller of the company's affairs. He is not a servant.'

2. Qualification

The Companies Act, 2013 does not prescribe any qualification to become a director of a company. To become a director, one need not be a shareholder. The Articles of Association of a company prescribes qualifications for a person to be appointed as a director. To become a director —

i. He/She must be a natural person.

ii. Need not have academic qualification.

iii. Must be competent to contract (within the meaning of Sec.11 of the Indian Contract Act, 1872).

v. He must not have been disqualified on the ground of insolvency or conviction by court.

3. Appointment of Directors (Sec.152)

Section 152 of the Companies Act, 2013 provides for the provisions relating to appoint of Directors. It runs as follows –

(1) Where no provision is made in the articles of a company for the appointment of the first director, the subscribers to the memorandum who are individuals shall be deemed to be the first directors of the company until the directors are duly appointed and in case of a One Person Company an individual being member shall be deemed to be its first director until the director or directors are duly appointed by the member in accordance with the provisions of this section.

(2) Save as otherwise expressly provided in this Act, every director shall be appointed by the company in general meeting.

(3) No person shall be appointed as a director of a company unless he has been allotted the Director Identification Number under section 154 [or any other number as may be prescribed under section 153].

(4) Every person proposed to be appointed as a director by the company in general meeting or otherwise, shall furnish his Director Identification Number [or such other number as may be prescribed under section 153] and a declaration that he is not disqualified to become a director under this Act.

(5) A person appointed as a director shall not act as a director unless he gives his consent to hold the office as director and such consent has been filed with the Registrar within thirty days of his appointment in such manner as may be prescribed:

Provided that in the case of appointment of an independent director in the general meeting, an explanatory statement for such appointment, annexed to the notice for the general meeting, shall include a statement that in the opinion of the Board, he fulfils the conditions specified in this Act for such an appointment.

(6) (a) Unless the articles provide for the retirement of all directors at every annual general meeting, not less than two-thirds of the total number of directors of a public company shall:

(i) be persons whose period of office is liable to determination by retirement of directors by rotation; and

(ii) save as otherwise expressly provided in this Act, be appointed by the company in general meeting.

(b) The remaining directors in the case of any such company shall, in default of, and subject to any regulations in the articles of the company, also be appointed by the company in general meeting.

(c) At the first annual general meeting of a public company held next after the date of the general meeting at which the first directors are appointed in accordance with clauses (a) and (b) and at every subsequent annual general meeting, one-third of such of the

directors for the time being as are liable to retire by rotation, or if their number is neither three nor a multiple of three, then, the number nearest to one-third, shall retire from office.

(d) The directors to retire by rotation at every annual general meeting shall be those who have been longest in office since their last appointment, but as between persons who became directors on the same day, those who are to retire shall, in default of and subject to any agreement among themselves, be determined by lot.

(e) At the annual general meeting at which a director retires as aforesaid, the company may fill up the vacancy by appointing the retiring director or some other person thereto.

Explanation: For the purposes of this sub-section, "total number of directors" shall not include independent directors, whether appointed under this Act or any other law for the time being in force, on the Board of a company.

(7) (a) If the vacancy of the retiring director is not so filled-up and the meeting has not expressly resolved not to fill the vacancy, the meeting shall stand adjourned till the same day in the next week, at the same time and place, or if that day is a national holiday, till the next succeeding day which is not a holiday, at the same time and place.

(b) If at the adjourned meeting also, the vacancy of the retiring director is not filled up and that meeting also has not expressly resolved not to fill the vacancy, the retiring director shall be deemed to have been re-appointed at the adjourned meeting, unless:

(i) at that meeting or at the previous meeting a resolution for the re-appointment of such director has been put to the meeting and lost;

(ii) the retiring director has, by a notice in writing addressed to the company or its Board of directors, expressed his unwillingness to be so re-appointed;

(iii) he is not qualified or is disqualified for appointment;

(iv) a resolution, whether special or ordinary, is required for his appointment or re-appointment by virtue of any provisions of this Act; or

(v) section 162 is applicable to the case.

Explanation: For the purposes of this section and section 160, the expression "retiring director" means a director retiring by rotation.

The Directors of a company may be appointed in any one of the following ways:

1. By the Articles of Association as first directors.
2. By the Company in Annual General Meeting.
3. By the Board of Directors.
5. By Lenders.
6. By the Central Government.

1. By The Articles of Association as First Directors: The first directors of a newly formed company are to be appointed by the subscribers of the memorandum. If they do not appoint any, all the subscribers who are individuals become directors. They hold office up to the date of the date of the first annual general meeting of the company where in appointment of directors is made.

2. By the Company in Annual General Meeting: According to Sec.255 directors of a company are to be appointed at its annual general meetings. It has been noted above the two subscribers of the memorandum, who are the first directors, continue until the directors are appointed at the general meeting.

In the case of a public company or its subsidiary private company, at least 2/3rd of the directors shall retire by rotation, and only up to 1/3rd of the total number of the directors can be permanent. The articles of a company may, however, provide that there will be no permanent directors, and all the directors shall retire at every annual general meeting.

At a general meeting 1/3rd or nearest to 1/3rd in number shall retire from office. Those who have been longest in office retire first.

As between persons who became directors on the same day the retirement may be in accordance with any mutual agreement between themselves. But, if there is no such agreement retirement shall be determined by lot.

3. By the Board of Directors: The general power to appoint directors is vested in the general meeting of the shareholders/ members but in two cases the Board of Directors can also appoint new directors.

According to Section 161 of the Companies Act, the Articles of Association empowers the Directors to appoint additional directors. Any additional directors appointed by the directors shall hold office only up to the date of the next annual general meeting of the company. The number of directors and additional directors must not exceed the maximum strength fixed for the Board by the Articles [*Patrakola Tea Co. Re*, AIR (1967) Cal. 406].

Section 161authorises the directors to fill casual vacancies. A casual vacancy occurs when the office of the director is vacated before the expiry of his term. Any person who is appointed by the Board in casual vacancy holds office until the expiry of the period for which the outgoing director would have held office. But additional directors shall hold office only up to the date of the next annual general meeting.

5. By Lenders(Sec. 161(3)): Under certain conditions the articles may empower the debenture holders, a banking company or a financial corporation to appoint their nominees to the Board of Directors. The number of the directors so appointed must not exceed one-third of the total strength of the Board of Directors.

6. By the Central Government: The Central Government may appoint directors in the exercise of its powers to prevent oppression or mismanagement. The Central Government can make such appointments on its own motion or on the application of at least hundred members or members holding not less than one-tenth of the total voting power. The appointment of such directors may be made for a period not exceeding three years at a time.

4. Disqualifications of Directors (Section 164)

Section 164 of the Companies Act, 2013 provides that the following persons are not eligible and shall not be appointed as director of any company:

a) a person certified by a Court of competent jurisdiction to be of unsound mind;

b) an un-discharged insolvent;

c) a person who has applied to be adjudicated as an insolvent and his application is pending; or

d) a person who has been convicted by a Court for any offence whether involving moral turpitude or other wise and sentence in respect thereof to imprisonment of not less than six months and a period of five years has not elapsed from the date of the expiry of the sentence:

Provided that if a person has been convicted of any offence and sentenced in respect thereof to an imprisonment for a period of seven years or more, he shall not be eligible to be appointed as a director in any company;

e) a person has been disqualified from being appointed as a director by an order of a Court or Tribunal and the order is in force; or

f) a person has not paid any calls in respect of shares of the company held by him and six months have elapsed from the last day fixed for the payment of the call; or

g) a person has been convicted of an offence dealing with related party transactions under Section 188 at any time during the last preceding five years; or

h) he has not complied with the provisions of sub-section (3) of Section 152 of the Companies Act, 2013;

(2) No person who is or has been a director of a company which-

(a) has not filed financial statements or annual returns for any continuous period of three financial years; or

(b) has failed to repay the deposits accepted by it or pay interest thereon or to redeem any debentures on the due date or pay interest due thereon or pay any dividend declared and such failure to pay or redeem continues for one year or more,

shall be eligible to be re-appointed as a director of that company or appointed in other company for a period of five years from the date on which the said company fails to do so.

Provided that where a person is appointed as a director of a company which is in default of clause (a) or clause (b), he shall not incur the disqualification for a period of six months from the date of his appointment.

ii) Provided that the disqualifications referred to in clauses (d), (e) and (g) of sub-section (1) shall continue to apply even if the appeal or petition has been filed against the order of conviction or disqualification.

A private company which is not a subsidiary of a public company may, by its Articles, provide that a person shall be disqualified for appointment as a director on any additional grounds.

A director who has been removed from office by the Central Government shall not be a director of any company for a period of 5 years from the date of removal.

5. Kinds of Directors

Directors of a company may be classified under the following heads –

1. First Directors.
2. Directors.
3. Additional Directors.
4. Alternative Director.
5. Nominee Director.
6. Director appointed by Casual Vacancy, and
7. Independent Director.

1. First Directors: As per Section 152(1) of the Companies Act, 2013, the first directors of a company are to be appointed by the subscribers of the memorandum. They are generally listed in the articles of the company. If they do not appoint any, all the subscribers who are individuals become directors. The very fact of incorporation makes them the first directors of the company. The first directors however hold office only up to the date of the first annual general meeting of the company.

2. Directors (Elected Directors): According to Section 152(2) of the Companies Act, 2013, every director shall be appointed by the company in general meeting.

3. Additional Directors: As per Section 161(1) of the Companies Act, 2013 the articles of a company may confer on its Board of Directors the power to appoint any person, other than a person who fails to get appointment as a director in a general meeting as an additional director at any time who shall hold office up to the date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier.

4. Alternative Director: According to Section 161(2) of the Companies Act, 2013, the Board of Directors of a company may, if so authorized by its articles or by a resolution passed by the company in general meeting, appoint a person, not being a person holding any

alternate directorship for any other director in the company; [or holding directorship in the same company] to act as an alternate director for a director during his absence for a period of not less than three months from India.

5. Nominee Director: According to Section 161(3) of the Companies Act, 2013, subject to the article of a company, the Board may appoint any person as a director nominated by any institution in pursuance of the provisions of any law for the time being in force or of any agreement or by the Central Government or the State Government by virtue of its share holding in a Government Company.

6. Director appointed in Casual Vacancy: As per Section 161(4) of the Companies Act, 2013, [xxx] if the office of any director appointed by the company in general meeting is vacated before his term of office expires in the normal course, the resulting casual vacancy may, in default of and subject to any regulations in the articles of the company, be filled by the Board of Directors at a meeting of the Board [which shall be subsequently approved by members in the immediate next general meeting].

7. Independent Director: As per Section 2(47) of the Companies Act, 2013 'independent director' means an independent director referred to in sub-section (6) of Section 149.

Sub-sections (6) to (13) of Section 149 of the Companies Act, 2013 read:

(6) An independent director in relation to a company, means a director other than a managing director or a whole-time director or a nominee director:

(a) who, in the opinion of the Board, is a person of integrity and possesses relevant expertise and experience;

(b) (i) who is or was not a promoter of the company or its holding, subsidiary or associate company;

(ii) who is not related to promoters or directors in the company, its holding, subsidiary or associate company;

(c) who has or had no [pecuniary relationship, other than remuneration as such director or having transaction not exceeding ten per cent. of his total income or such amount as may be prescribed,] with the company, its holding, subsidiary or associate company, or their promoters, or directors, during the two immediately preceding financial years or during the current financial year;

[(d) none of whose relatives—

(i) is holding any security of or interest in the company, its holding, subsidiary or associate company during the two immediately preceding financial years or during the current financial year:

Provided that the relative may hold security or interest in the company of face value not exceeding fifty lakh rupees or two per cent. of the paid-up capital of the company, its holding, subsidiary or associate company or such higher sum as may be prescribed;

(ii) is indebted to the company, its holding, subsidiary or associate company or their promoters, or directors, in excess of such amount as may be prescribed during the two immediately preceding financial years or during the current financial year;

(iii) has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, its holding, subsidiary or associate company or their promoters, or directors of such holding company, for such amount as may be prescribed during the two immediately preceding financial years or during the current financial year; or

(iv) has any other pecuniary transaction or relationship with the company, or its subsidiary, or its holding or associate company amounting to two per cent. or more of its gross turnover or total income singly or in combination with the transactions referred to in sub-clause (i), (ii) or (iii);]

(e) who, neither himself nor any of his relatives:

(i) holds or has held the position of a key managerial personnel or is or has been employee of the company or its holding, subsidiary or associate company in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed;

[Provided that in case of a relative who is an employee, the restriction under this clause shall not apply for his employment during preceding three financial years.]

(ii) is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed, of:

(A) a firm of auditors or company secretaries in practice or cost auditors of the company or its holding, subsidiary or associate company; or

(B) any legal or a consulting firm that has or had any transaction with the company, its holding, subsidiary or associate company amounting to ten per cent. or more of the gross turnover of such firm;

(iii) holds together with his relatives two per cent. or more of the total voting power of the company; or

(iv) is a Chief Executive or director, by whatever name called, of any non-profit organisation that receives twenty-five per cent. or more of its receipts from the company, any of its promoters, directors or its holding, subsidiary or associate company or that holds two per cent. or more of the total voting power of the company; or

(f) who possesses such other qualifications as may be prescribed.

(7) Every independent director shall at the first meeting of the Board in which he participates as a director and thereafter at the first meeting of the Board in every financial year or whenever there is any change in the circumstances which may affect his status as an independent director, give a declaration that he meets the criteria of independence as provided in sub-section (6).

Explanation: For the purposes of this section, "nominee director" means a director nominated by any financial institution in pursuance of the provisions of any law for the time being in force, or of any agreement, or appointed by any Government, or any other person to represent its interests.

(8) The company and independent directors shall abide by the provisions specified in Schedule IV.

(9) Notwithstanding anything contained in any other provision of this Act, but subject to the provisions of sections 197 and 198, an independent director shall not be entitled to any stock option and may receive remuneration by way of fee provided under sub-section (5) of section 197, reimbursement of expenses for participation in the Board and other meetings and profit related commission as may be approved by the members.

(10) Subject to the provisions of section 152, an independent director shall hold office for a term up to five consecutive years on the Board of a company, but shall be eligible for re-appointment on passing of a special resolution by the company and disclosure of such appointment in the Board's report.

(11) Notwithstanding anything contained in sub-section (10), no independent director shall hold office for more than two

consecutive terms, but such independent director shall be eligible for appointment after the expiration of three years of ceasing to become an independent director:

Provided that an independent director shall not, during the said period of three years, be appointed in or be associated with the company in any other capacity, either directly or indirectly.

Explanation: For the purposes of sub-sections (10) and (11), any tenure of an independent director on the date of commencement of this Act shall not be counted as a term under those sub-sections.

(12) Notwithstanding anything contained in this Act,—

(i) an independent director;

(ii) a non-executive director not being promoter or key managerial personnel,

shall be held liable, only in respect of such acts of omission or commission by a company which had occurred with his knowledge, attributable through Board processes, and with his consent or connivance or where he had not acted diligently.

(13) The provisions of sub-sections (6) and (7) of section 152 in respect of retirement of directors by rotation shall not be applicable to appointment of independent directors.

6. Position of Directors

It is very difficult to define the exact position of directors. A director is an officer of the Company. He is a manager, controller of the company. Bowen L.J. in *Imperial Hydropathic Co. vs. Hampson*, (1882) 23 Ch.D.1 – opined that, directors are described sometimes as 'Agents', sometimes 'Trustees' and sometimes as 'Managing Partners'. The position of Directors may be well explained with reference to the following heads.

1. Directors as Agents.
2. Directors as Employees.
3. Directors as Officers.

4. Directors as Trustees.
5. Director as Organ; and
6. Power and Duties of the Directors.

1. Directors as Agents: A company being an artificial person cannot act by itself. It acts through the Agents called 'Directors'. Hence, the relationship between company and Director is that of Principal and Agent. The true position of directors seems to be that of agents for the company with powers and duties of carrying on the whole of its business subject to the restrictions imposed by the Articles and the statutory provisions. But the directors of company are not agents for the share-holders. If the Director enters into a contract with third party on behalf of the company, the company is liable (not the Director).

The important functions of the directors as agents of the company are to enter into contracts, to create negotiable instruments and to borrow money on behalf of the company. Besides, it is to be noted that notice to a director will amount to notice to the company if the director is bound in the course of his duty to receive the notice and to communicate it to the company.

2. Directors as Employees: The directors are not servants of the company or members of its staff. They cannot be treated as the employees of the company. However, in addition to his directorship, he may hold a salaried employment in the company and in such a condition he will enjoy all the rights available to an employee or servant of the company. However, even in such a case his rights as a director will be separate from his rights as an employee or servant of the company.

3. Directors as Officers: For certain matters under the Companies Act, the directors are treated as officers of the company. As such they are liable to certain penalties if the provisions of the Companies Act are not strictly complied with.

4. Directors as Trustees: Directors are described as the Trustees of the Company, particularly in respect of property and financial matters. Directors play an important role in issue or transfer

of shares, and making calls. Like trustee, protects the interest of beneficiary, Directors protect the interest of shareholders.

Joint Stock Discount Co. v. Brown (1869) 8 EQ. 376) – In this case, the Directors of the Company had misapplied/ misappropriated the funds of the company. It was held that it amounts to breach of trust and hence, the directors are held jointly and severally liable.

Lindley, L.J. in re *Lands Allotment Co.* (1893) 1 Ch. 617 observes that 'although directors are not properly speaking trustees, yet they have always been considered and treated as trustees of money which comes to their hands or which is actually under their control; and ever since joint stock companies were invented directors have been held liable to make good moneys which they have misapplied upon the same footing as if they were trustees.

Another reason why the directors have been described as trustees is because of the peculiar nature of their office. The directors are persons selected to manage the affairs of the company for the benefit of the shareholders. It is an office of trust, which, if they undertake, it is their duty to perform fully and entirely. Some of their duties towards the company are of the same nature as those of a trustee.

The Madras High Court in *RamaswamyIyer v. Brahmayyà& Co.* (1966) 1 Comp. LJ. 107 Mad) observed that –It is settled view that for the company the directors of a company are trustees.

The directors, with reference to their entrusted power of applying money and property of the company and for misuse of the power, could be rendered liable as trustees and on their death, even the cause of action survives against their legal successors.

Yet the directors are not trustees in the real sense because a trustee cannot take any advantage from the trust property while directors receive dividend and remuneration from the company.

5. Director as Organ: In the eyes of law there are two types of persons, i.e. artificial persons and natural persons. A company being an artificial person has to be managed and controlled by natural

persons. These natural persons are directors of company. They are the brain and mind of the artificial persons, i.e. the company.

According to Neville, J. – Man uses his bodily organs for a purpose, Corporation uses men. The Board of Directors are the brain and the brain only of the company, which is the body and the company can and does act only through them. (*Bath v. Standard Land Co*. (1910) 2 Ch. 408).

Therefore, a company has no physical existence and hence, it operates through the Board of Directors who is considered to be the brain and the only brain of the company. In Bath vs. Standard Land Company, Neville J. observed that the Board of Directors are the brain and the only brain of the company which is the body and the company can and does act only through them.

In *H.L.Botton Engineering Co. Ltd. v. T.J.Graham& Sons,* Denning, J. has observed that the directors and manager represent the directing mind or will of the company. The state of mind is the mind of the company.

Lord Justice Denning rightly said in *Bolton (Engineering) Co. Ltd. v. Graham & Sons* (1957) 1 QB 159 CA – "A company may in many ways be likened to a human body. It has a brain and nerve centre which controls what it does. It also has hands which hold the tools and act in accordance with the directions from the centre. Some of the people in the company are mere servants and agents who are nothing more than hands to do the work and cannot be said to represent the mind or will. Others are directors and managers who represent the directing mind and will of the company, and control what it does. The state of mind of these managers is the state of mind of the company and is treated by the law as such."

Thus, it was held that it is sufficient to show that the Board of Directors is the mind of corporate body.

Further, it is stated that the organic theory of corporate personality treats directors as organs of the company for whose action the company is to be held liable just as a natural person is for the action of his limbs.

Conclusion: The directors are neither agents nor trustees of the company exclusively but they are agents and trustees both. They are agents in respect of the transactions which they enter into on behalf of the company and they are trustees of the company" money and property and also of the powers which they are authorised to exercise on behalf of the company. It would be better to say that the directors stand in fiduciary relationship with the company. As fiduciaries they are required to display utmost good faith towards the company in their dealings with it. They must exercise their power bona fide in the interest of the company and for the particular purpose for which the powers are given to them and not for some extraneous purpose. On account of such fiduciary position, they are prohibited to place themselves in a position in which there is conflict between their duties and their personal interest.

7. Powers of Directors (Section 179)

Section 179 of the Companies Act, 2013 (Corresponding to Sections 291 and 292 of the Companies Act, 1956) deals with the powers of the Board of Directors. It runs as follows:

Powers of Board of Directors (Sec.179):

Powers of Board:— (1) The Board of Directors of a company shall be entitled to exercise all such powers, and to do all such acts and things, as the company is authorised to exercise and do:

Provided that in exercising such power or doing such act or thing, the Board shall be subject to the provisions contained in that behalf in this Act, or in the memorandum or articles, or in any regulations not inconsistent therewith and duly made thereunder, including regulations made by the company in general meeting:

Provided further that the Board shall not exercise any power or do any act or thing which is directed or required, whether under this Act or by the memorandum or articles of the company or otherwise, to be exercised or done by the company in general meeting.

(2) No regulation made by the company in general meeting shall invalidate any prior act of the Board which would have been valid if that regulation had not been made.

(3) The Board of Directors of a company shall exercise the following powers on behalf of the company by means of resolutions passed at meetings of the Board, namely:

(a) to make calls on shareholders in respect of money unpaid on their shares;

(b) to authorise buy-back of securities under section 68;

(c) to issue securities, including debentures, whether in or outside India;

(d) to borrow monies;

(e) to invest the funds of the company;

(f) to grant loans or give guarantee or provide security in respect of loans;

(g) to approve financial statement and the Board's report;

(h) to diversify the business of the company;

(i) to approve amalgamation, merger or reconstruction;

(j) to take over a company or acquire a controlling or substantial stake in another company;

(k) any other matter which may be prescribed:

Provided that the Board may, by a resolution passed at a meeting, delegate to any committee of directors, the managing director, the manager or any other principal officer of the company or in the case of a branch office of the company, the principal officer of the branch office, the powers specified in clauses (d) to (f) on such conditions as it may specify:

Provided further that the acceptance by a banking company in the ordinary course of its business of deposits of money from the public repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise, or the placing of monies on deposit by a banking company with another banking company on such conditions as the Board may prescribe, shall not be deemed to be a borrowing of monies or, as the case may be, a making of loans by a banking company within the meaning of this section.

Explanation I: Nothing in clause (d) shall apply to borrowings by a banking company from other banking companies or from the Reserve Bank of India, the State Bank of India or any other banks established by or under any Act.

Explanation II: In respect of dealings between a company and its bankers, the exercise by the company of the power specified in clause (d) shall mean the arrangement made by the company with its bankers for the borrowing of money by way of overdraft or cash credit or otherwise and not the actual day-to-day operation on overdraft, cash credit or other accounts by means of which the arrangement so made is actually availed of.

(4) Nothing in this section shall be deemed to affect the right of the company in general meeting to impose restrictions and conditions on the exercise by the Board of any of the powers specified in this section.

The Board of Directors derive their powers from two sources namely–

a) Articles of Association.

b) Companies Act, 2013.

The powers of Directors may be explained under the following heads:

1. General Powers.
2. Powers exercised by the Board (of Directors) at its meetings.
3. Powers with the consent of shareholders in General Body Meeting.

1. General Powers (Sec.291): Directors exercise all powers as authorised by the Company. These powers are subject to the provisions of the Companies Act. Such powers should not be contrary to the contents in Memorandum and Articles, and also regulations of General Meeting.

Section 179 confers on Board of Directors, to exercise all such powers and do all such acts as the company is authorized to do. In other words, the powers of the Board of Directors are co-

extensive to that of the company under the Companies Act. The powers of the Directors are subject to the provisions and restrictions in the Memorandum and Articles of Association of the Company.

In *Automatic Self Cleaning Filter Syndicate Co. Ltd. v. Cunningham* (1906) 2 Ch. 34) – the company had power under its memorandum to sell its undertaking to another company having similar objects. The articles of the company contained a provision by which directors were empowered to sell or otherwise deal with the property of the company. The shareholders passed a simple resolution for the sale of the company's assets on certain terms and required the directors to carry out the sale. The directors refused to comply with the wishes of the shareholders whereupon it was contended on behalf of the shareholders that they were the Principal and directors being their agents were bound to give effect to their decision. The Court, however, rejected the plea of shareholders and held that directors are agents not of a majority of shareholders, but of the company which comprised whole entity of shareholders. Therefore, if the company has entrusted the directors with a particular power, a simple majority could not interfere in exercise of it.

The Board of Directors are not entitled to exercise such powers, which are expressly vested in the shore holders. Relevant case on this point is – *Srinivasan v. Subramania* (AIR 1932 Mad 100), the directors were restrained from exercising a power which was expressly vested in the shareholders.

Exceptions: The powers vested in the Board of Directors can be out *weighted/setaside* by the majority shareholders (by special resolution in the general meeting) in the following exceptional cases –

1. Where the directors act *mala fide* against the interest of the company, the members can reconstitute the Board.
2. Where the Board for some valid reasons becomes *incompetent* to act. For example, if the personal interest of the directors is in conflict with their duty.

3. When there is a *dead-lock* in the Board i.e. when the members of the Board are equally divided on a particular issue.

2. Powers exercised by the Board at its Meetings: According to Sec.179, the Board of Directors exercises the following powers:

a) to make calls against shares;

b) to issue debentures;

c) to borrow money;

d) to invest funds of the company; and

e) to make loans.

b) the power to issue debentures;

c) the power to borrow moneys otherwise than on debentures;

d) the power to invest the funds of the company; and

e) the power to make loans;

The Board may, however, by a resolution passed at a meeting, delegate the powers mentioned in clauses (c), (d) and (e) above to any committee of directors, the managing director, the manager or any other principal officer of the company.

In addition to the above mentioned powers to be exercised only at the Board meetings, there are some other powers which must also be exercised by the Board through its meeting. They are:–

a) Power to accord sanction for certain contracts in which particulars directors are interested (Section 188).

b) Power to appo8int or employ a person as managing director if he is already the managing director or manager of any other company (Sec.203).

c) Power to invest in any shares or debentures of any other body corporate up to ten per cent of the subscribed capital of such other body corporate, provided that the aggregate of the investments made by the company in all other bodies corporate

does not exceed thirty per cent of the subscribed capital of the investing company and provided further that the aggregate of the investments made in all bodies corporate in the same group does not exceed twenty per cent of the subscribed capital of the investing company (Sec.186).

d) Power to appoint or employ a person as its manager if he is already the manager or managing director of another company (Sec.203).

e) Power to make a declaration of solvency to make the winding up of a company as a members' voluntary winding up (Sec.305).

f) Receiving notice of disclosure of interest of directors (Sec.184).

3. Powers of Directors with the consent of shareholders: The Board of Directors can exercise powers with the consent of shareholders in the following cases.

1) Sale or lease of Company's undertaking.

2) Extension of time for payment of debt due by Director.

3) Investment of money received against compulsory acquisition of Company's assets.

4) Borrowing of money beyond paid up capital.

Duties and Liabilities of Directors

The Duties and Liabilities of Directors may be explained under the following heads:

1. Duties towards company.
2. Duty of care.
3. Duty to attend Meetings.
4. Duty not to delegate powers
5. Duty to disclose personal interest.
6. Duty to act honestly and in good faith.
7. Director's Duties to Individual Members.

8. Director's Duty towards third (other) persons.
9. Vacation of office by Director (Sec.167), and
10. Resignation by a Directors (Sec.168).

1. Duties towards company: Under the Companies Act directors are accountable for their acts done on behalf of the company. Besides the statutory duties which the directors have to perform to ensure strict compliance with the various provisions of the Act they also have certain duties which arise out of their fiduciary relationship with the company.

The duties of good faith and honesty arising out of the fiduciary relationship between the director and his company are analogous to those of a trustee. The law imposes these duties upon the directors so that they are not allowed to 'capitalise their strategic position in the company to serve their own interest.' The Australian Uniform Companies Act has incorporated statutory provisions containing an explicit reference to the fiduciary obligation of directors towards their companies. Section 124 of the Australian Uniform Companies Act states:

1. A director shall at all times act honestly and use reasonable diligence in the discharge of the duties of his office.
2. An officer (including a director) shall not make use of any information acquired by virtue of his position s an officer (director) to gain directly or indirectly any improper advantage for himself or to cause detriment to the company.

2. Duty of Care: The directors of a company are expected to perform their duties with utmost care, skill and attention. The Directors have fiduciary relationship with the company and are liable for breach of duty of care. A director is required to perform his duties and obligations with skill and diligence as expected from a reasonable person of his knowledge and experience. The directors of a company, while discharging their duties must exercise some degree of skill and diligence but he does not owe to his company the duty to take all possible care or to act with best care.

Where a director acts within his powers, he cannot be held liable for mistakes or errors of judgment even if it causes loss to the company provided he has acted bona fide for the benefit of the company and with such care and caution as may reasonably be expected from a man of his knowledge and experience.

In **Re City Equitable Fire Insurance Co. (1925) 1 Ch. 407** – In this case, the company collapsed due to bad investments and bad debts and misappropriation caused by fraudulent acts of a director. The company suffered a loss to the tune of £ 12,00,000 and eventually was ordered to be wound up. The director was convicted for his fraud and negligence. He was, however, acquitted in appeal because of an exception clause in the articles to hold directors liable only for gross negligence.

In *Jorchester Finance Co. Ltd. v. Stebbing* (1989) BLC 498) – it has been held that the duty of care extends uniformly to all the directors whether they are executive or non-executive directors. Thus the two non-executive directors of a company were held liable for the loss caused to the company due to their negligence in signing blank cheques which enables the executive directors to enter the amount as they pleased in those cheques.

The High Court of Bombay in *Harish Chandra Maganlal v. Union of India* (AIR 1990 Bom. 34(36) – pointed out that the law makes no difference between whole-time directors and part-time directors in the matter of liability arising from their negligence or breach of duty excepting that in case of part-time directors, they can be more readily relieved from liability when it is proved that they had no active role in the management of the company.

3. Duty to attend meetings: A director is ought to attend all meetings. However, he is not bound to attend all meetings. If a Director habitually abstains from the meetings, he is liable for the acts of his co-directors. According to Section 167(1)(b), if a Director absents himself from three consecutive meetings of the Board for a continuous period of twelve months, he is liable to vacate his office.

In **Re, Denham & Co. (19893) 25 Ch.D. 752** – The articles conferred on all the powers of the Board of Directors on the

Chairman. A director attended no meeting of the Board for four years, but he was held not to be liable for fraudulent reports and balance sheets issued and passed by his co-directors for dividend paid by them. This is a case of unusual nature because normally the articles do not confer all the powers of directors on the Chairman.

In **Marquis of Bute, (1892) 2 Ch. 100 –** There were 50 trustees (person in position of directors). One of the trustees attends no meeting for a longer period but he was not held liable for the misconduct of his 'co-directors'. This is also a case of unusual nature because normally the companies do not have such a large number of directors.

4. Duty, not to delegate powers: Delegation of power means transferring power to another, the subordinates. The Director acts on behalf of the company, is a delegate. A Director, being a delegate cannot further delegate his power. This rule/principle is enshrined in the maxim 'delegates non protest delegate'.

However, a director may delegate his functions under the following circumstances.

a) If the Companies Act or the articles of the company permits a delegation of functions.

b) If the delegation is necessary in the ordinary course of the business of the company, certain duties of a director may, having regard to the exigencies of business, properly be left to some other official.

***Dovey v. Cory* (1901) AC 477,** is a leading case on this point. In this case a bank had sustained heavy losses on account of the issue of fraudulent balance sheets and advances of money to the customers of the bank on improper security. The frauds were the work of the manager and Chairman. The manager and Chairman manipulated the account and showed a profit, while in fact there was no profit.

At a meeting of the Board, a Director (Cory) was ensured of the correctness of the account and on the assurance and advice of

the manager and Chairman, he assented to the payment of dividend which was in reality paid out of the capital.

The question arose whether the Director (Cory), who was in fact innocent was also liable to the company for negligence in not having discovered the frauds.

The House of Lords exonerated him (Cory) from liability on the ground that he had acted on representations made to him by the Chairman and General Manager on whose Judgment and information he was entitled to rely as he had no grounds for suspicion of their integrity or competence.

'I think he was entitled to rely upon the judgment, information and advice of the Chairman and General Manager as to whose integrity, skill and competence he had no reason for suspicion.'

In *D.Doss v. C.P.Connel*, AIR 1933 Mad. 124, an undischarged insolvent was appointed as an advisory director of a company. He misappropriated a part of the security money received from the company's employees. His co-directors were held not liable for the misappropriation because they had no reason to suspect his integrity and honesty.

5. Duty to disclose personal interest (Sec.184): Section 184 of the Companies Act, 2013 (corresponding to Section 299 of the Companies Act, 1956) lays down the procedure relating to director's duty to disclose personal interest. The relationship between director and the company being that of an agent and a principal, the former occupies a fiduciary position toward the latter. Therefore, directors are under a duty to ensure that their personal interests do not clash with those of the company's interests. The law expects a director to discharge his duties towards the company without any personal interest of his own.

A Director has a duty to disclose in case he received any profit or gain in connection with sale or purchase of any company's property or by selling his own property to the company. Section 184 requires every director who is interested in any transaction of the company to disclose his interest to the Board of Directors at its

meeting. The disclosure must be made at the first meeting of the Board held after the director has become so interested.

As to the question what constitutes an 'interest' for the purposes of Section 299 of the Companies Act, 1956 (now Section 184 of the Companies Act, 2013) the Courts have ruled that it should be a kind of personal interest which clashes with the duties of director towards his company. Thus where the directors participated and voted at a meeting of the Board which granted debentures to two of them, the resolution was held to be void as it involved personal interest of the participating directors (In *Re North-Eastern Insurance Co. Ltd.* (1919) 1 Ch. 198).

The Delhi High Court in *M/s.RajCylendars& Containers v. Hindustan General Industries Ltd.* (AIR 1998 Del. 418)l has observed that where the directors are personally interested in the deal, the contract is to the detriment of the company and hence not binding on it. In the instant case the defendant company entered into a contract with the plaintiff company to sell some machineries with the plaintiff on 'no profit no loss' basis. The Directors of the defendant company wanted to purchase some shares of their company from the Directors of the plaintiff company and perhaps it is for this reason that they allowed the concession of 'no profit no loss' to the plaintiff company. The Court held tht this transaction was done by the Directors of both the companies in their individual capacity and the plaintiff company was not a party to that contract because there was ;no mention in the resolution authorizing the Managing Director that the suit should also be instituted against the directors of the defendant company. Therefore, the terms and conditions could not be deemed to be binding on the defendant company particularly when the said conditions could not be deemed to be binding on the defendant company particularly when the said conditions were detrimental to Defendant Company. Hence the defendant company was not bound by the contract.

The directors owe a duty not only to the company but also to its creditors to ensure that the property of the company is not exploited for the benefit of the directors themselves and the interests of creditors

are not jeopardized (In *Re Winkworth Edward Baron Development Co.Ltd.* (1987) 1 All ER 114).

6. Duty to act in good faith: The expression 'good faith' means, "duty to disclose all material facts or not to supress any material facts for selfish ends." The directors are not only the agents but also the trustees of the company, and therefore, they have a duty to observe the principle of good faith. They should not do anything, which results in any personal benefit to them at the cost of the company. If the directors purchase such shares, which ought to have been purchased by the company and make a personal profit by selling those shares, they are bound to account for the profit to the company.

The relevant case on this point:

***Cook v. Deeks*(1916) 1 AC 554** – In this case, the Directors managed to get railway contract in their own name (not in company's name). Held that the Directors can not get any benefit under the contract and must give it to the company.

7. Director's duties to Individual Members: It must be stated that directors owe a duty to their company but not to individual members while carrying out transactions with such members, whether the directors act on behalf of the company or on behalf of themselves *(Multinational Gas & Petrochemical Co. v. Multinational Gas & Petrochemical Services Ltd.* (1983) 2 All ER 563). It is well settled that directors are not trustees for individual share holders (*National Zaver v. Bombay Life Insurance Co. Ltd.* (1950) 20 Comp. Cas 179 SC). Therefore, directors who purchase shares from members of their company are under no obligation to disclose information which they have which might induce the members to demand higher price *(Percival v. Wright* (1902) 2 Ch. 421). However, if the directors induce the members to sell their shares at a low price by misleading them as to the actual value of shares, they would certainly be held liable and the members can claim damages for the loss sustained by them.

Though generally speaking, directors owe no fiduciary duty to the members but in certain situations they do owe a duty to exercise

reasonable skill and care in advising members about a particular transaction relating to the company or its undertaking. Thus where a takeover bid is made for a company; the directors owe a fiduciary duty to render advice honestly to the share holders to whom the bid is addressed along with a duty to advise the company (*Gething v. Kilner* (1972) 1 All ER 166).

8. Director's duty to third (other) persons: It is true that the directors are not personally liable for the contracts entered into by third parties with the company; instead the company is held liable for such transactions. Likewise if the contracts entered into by company are *ultra-vires* the company, then also directors shall not be liable because such contracts are void in law (*Furguson v. Wilson* (1866) 2 Ch 77). But if the director enters into a contract with a third person in his own name suppressing the fact that he is doing so in his capacity as a director of that company, in that case he shall be personally liable to any loss caused to the company on account of that contract.

Where a director is guilty of fraud or deceit or commits a tort in relation to a company's transaction, he shall be personally liable to pay compensation to the person or persons who sustain damages because of such transactions. He shall also be liable for omissions which cause damages to third party.

The directors may be held criminally liable for acts or transactions of the company which constitute an offence under the Indian Penal Code. Thus in *U.P.Pollution Control Board v. Modi Distillery* (AIR 1988 SC 128) the directors of the company along with the managing director and chairman of an industrial unit were prosecuted for willful default in furnishing details regarding anti-pollution measures adopted by the unit. The Court held that where an offence has been committed by the company, every person who at the time of the commission of the offence was in charge and responsible to the company for the conduct, shall be liable.

Directors may be held personally liable to third parties under the Companies Act in the following circumstances:

i) where they issued a prospectus which did not contain the particulars required by the Act; or

ii) for misrepresentation in the prospectus; or

iii) where an irregular allotment was made; or

iv) where the company is unable to allot shares within 30 days of the first issue of the prospectus, and money received from applicants for shares has not been repaid within next 15 days; or

v) where the company is being wound up, the directors may be made liable for detbs of the company incurred through fraudulent transactions by directors on behalf of the company.

Apart from the Companies Act, directors may also incur personal liability to third persons for breach of implied warranty of authority for acts which although *intra vires* the company is outside the scope of their own authority as defined in the articles. Where a director acts in his own name instead of the company's name, he shall be personally liable to the third party for damages resulting from such acts.

9. Vacation of Office by Director (Sec.167): Section 167 of the Companies Act, 2013 (Corresponding to Section 283 of the Companies Act, 1956) lays down the rules relating to vacation of office by director of a company. It runs as follows –

1. The office of a director shall become vacant in case –

a) He incurs any of the disqualifications specified in Section 164;

Provided that where he incurs disqualification under sub-section (2) of section 164, the office of the director shall become vacant in all the companies, other than the company which is in default under that sub-section.

b) He absents himself from all the meetings of the Board of Directors held during a period of twelve months with or without seeking leave of absence of the Board;

c) He acts in contravention of the provisions of Section 184 relating to entering into contracts or arrangements in which he is directly or indirectly interested;

d) He fails to disclose his interest in any contract or arrangement in which he is directly or indirectly interested, in contravention of the provisions of Section 184;

e) He becomes disqualified by a order of a court or the Tribunal;

f) He is convicted by a court of any offence, whether involving moral turpitude or otherwise ad sentenced in respect thereof to imprisonment for not less than six months:

Provided that the office shall not be vacated by the director in case of orders referred to in clauses (e) and (f)-

(i). for thirty days from the date of conviction or order of disqualification;

(ii) where an appeal or petition is preferred within thirty days as aforesaid against the conviction resulting in sentence or order, until expiry of seven days from the date on which such appeal or petition is disposed of; or

(iii) where any further appeal or petition is preferred against order or sentence within seven days, until such further appeal or petition is disposed of.;

g) He is removed in pursuance of the provisions of this Act;

h) He, having been appointed a director by virtue of his holding any office or other employment in the holding, subsidiary or associate company, ceases to hold such office or other employment in that company.

2. If a person, functions as a director even when he knows that the office of director held by him has become vacant on account of any of the disqualifications specified in sub-section (1), he shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees, or with both.

3. Where all the directors of a company vacate their offices under any of the disqualifications specified in sub-section (1), the promoter or, in his absence, the Central Government shall appoint the required number of directors who shall hold office till the directors are appointed the required number of directors who shall hold office till the directors are appointed by the company in the general meeting.

4. A private company may, by its articles, provide any other ground for the vacation of the office of a director in addition to those specified in sub-section (1).

The office of the Director of a company stands vacated under the following situations.

1. Disqualification specified in Section 164: If he/she incurs any of the disqualification specified in Section 164 such as unsound mind, undischarged insolvent, pending adjudication of insolvency, conviction, related party transaction, failure to file financial statement and disqualifying order passed by the Court/Tribunal.

2. Absence from Board of Director's Meeting: He/she absents/herself from all meeting of the Board of Directors held during a period twelve month with or without seeking leave of absence of the Board.

3. Contract involving period interest: He/she entered into contract/agreement in which his/her personal interest is involved.

4. Contract – Non-disclose of interest: He/she fails to disclose his/her interest in any contract/arrangement.

5. Disqualification by order of Court/Tribunal: He/she becomes disqualified by a order of a Court/Tribunal.

6. Conviction: He/she convicted by a Court for any offence whether involving moral turpitude or otherwise and sentenced in respect thereof to imprisonment for that less than six months. The officer of such director shall stand vacated even if he/she preferred appeal against such conviction.

7. Knowledge of vacation of office: The office of the Director shall stand vacated in case such delinquent director continues in office, despite of having knowledge that the his/her tenure of office is expired.

10.Resignation by a Directors (Sec. 168): Section 168 prescribes procedure for resignation from office by director of a company. It runs as follows –

Resignation of director— (*1*) A director may resign from his office by giving a notice in writing to the company and the Board shall on receipt of such notice take note of the same and the company shall intimate the Registrar in such manner, within such time and in such form as may be prescribed and shall also place the fact of such resignation in the report of directors laid in the immediately following general meeting by the company:

Provided that a director may also forward a copy of his resignation along with detailed reasons for the resignation to the Registrar within thirty days of resignation in such manner as may be prescribed.

(2) The resignation of a director shall take effect from the date on which the notice is received by the company or the date, if any, specified by the director in the notice, whichever is later:

Provided that the director who has resigned shall be liable even after his resignation for the offences which occurred during his tenure.

(3) Where all the directors of a company resign from their offices, or vacate their offices under section 167, the promoter or, in his absence, the Central Government shall appoint the required number of directors who shall hold office till the directors are appointed by the company in general meeting.

Removal of Directors (Sec. 169): Section 169 of the Companies Act, 2013 (Corresponding to Section 284 of the Companies Act, 1956) lays down the procedure for removal of a director. It reads as follows –

(1) A company may, by ordinary resolution, remove a director, not being a director appointed by the Tribunal under section 242, before the expiry of the period of his office after giving him a reasonable opportunity of being heard:

Provided that nothing contained in this sub-section shall apply where the company has availed itself of the option given to it under section 163 to appoint not less than two thirds of the total number of directors according to the principle of proportional representation.

(2) A special notice shall be required of any resolution, to remove a director under this section, or to appoint somebody in place of a director so removed, at the meeting at which he is removed.

(3) On receipt of notice of a resolution to remove a director under this section, the company shall forthwith send a copy thereof to the director concerned, and the director, whether or not he is a member of the company, shall be entitled to be heard on the resolution at the meeting.

(4) Where notice has been given of a resolution to remove a director under this section and the director concerned makes with respect thereto representation in writing to the company and requests

its notification to members of the company, the company shall, if the time permits it to do so:

(*a*) in any notice of the resolution given to members of the company, state the fact of the representation having been made; and

(*b*) send a copy of the representation to every member of the company to whom notice of the meeting is sent (whether before or after receipt of the representation by the company),

and if a copy of the representation is not sent as aforesaid due to insufficient time or for the company's default, the director may without prejudice to his right to be heard orally require that the representation shall be read out at the meeting:

Provided that copy of the representation need not be sent out and the representation need not be read out at the meeting if, on the application either of the company or of any other person who claims to be aggrieved, the Tribunal is satisfied that the rights conferred by this sub-section are being abused to secure needless publicity for defamatory matter; and the Tribunal may order the company's costs on the application to be paid in whole or in part by the director notwithstanding that he is not a party to it.

(*5*) A vacancy created by the removal of a director under this section may, if he had been appointed by the company in general meeting or by the Board, be filled by the appointment of another director in his place at the meeting at which he is removed, provided special notice of the intended appointment has been given under sub-section (*2*).

(*6*) A director so appointed shall hold office till the date up to which his predecessor would have held office if he had not been removed.

(*7*) If the vacancy is not filled under sub-section (*5*), it may be filled as a casual vacancy in accordance with the provisions of this Act:

Provided that the director who was removed from office shall not be re-appointed as a director by the Board of Directors.

(8) Nothing in this section shall be taken:

(*a*) as depriving a person removed under this section of any compensation or damages payable to him in respect of the termination of his appointment as director as per the terms of contract or terms of his appointment as director, or of any other appointment terminating with that as director; or

(*b*) as derogating from any power to remove a director under other provisions of this Act.

As per Section 242(2)(h), of the Companies Act, 2013 without prejudice to the generality of the powers under sub-section (1), an order under that sub-section may provide for removal of the managing director, manager or any of the directors of the company.

The Directors of a company may be removed by –

1. By company in General Meeting (Share-holders) and
2. By the Tribunal.

1. Removal by Company in General Meeting (Shareholders): Section 169 of the Companies Act, 2013 (Corresponding to Section 284 of the Companies Act, 1956).

Shareholders: Provided that the members of a company may, by ordinary resolution remove a director before the expiry of his period of office, except in the following cases:

1. It does not apply in case of a director appointed by the Central Government.
2. It does not apply in the case of a private company, in which a director is holding office for life; and
3. It does not apply in case of a company which has opted to elect 2/3rd of its directors by the system of proportional representation.

Special notice must be given of the resolution to remove a director. A copy of it must be given to the director concerned. A statement relating to the matter may be sent by the director concerned, to the company and such statement shall be circulated

among the members, is received in time, or read out in the meeting. The circulation of such statement may be prohibited by court if it contains defamatory matter.

The meeting, which removes a director, can elect another in his place if the director was originally appointed by election.

If a director is, by agreement or otherwise entitled to receive compensation for premature termination of his services, he can enforce his claim notwithstanding the removal by resolution.

The Bombay High Court in *ParrelPutado v. State of Goa* (1994) 80 Comp. Cas 859 Bom.) has held that Section 284 of the Companies Act, 1956 i.e. removal of director by the shareholders (Corresponding Section 169 of the Companies Act, 2013), does not apply to nominated directors and those of a Government company. The matter of appointment and removal of directors is in realm of contract and thereafter cannot be challenged without jurisdiction.

The Punjab and Haryana High Court in *BhankapurSinbhaoli Beverages P. Ltd. v. P.R. Pandya* (1995) 17 Corpt. LA 170 P & W), held that a resolution for removing the director without affording the opportunity of making a representation would be null and void. Therefore, where there was no proof of a letter to the director sought to be removed, amounted a denial of opportunity.

Where the Articles of Association provide that a company may remove any director 'for negligence, misconduct or any other reasonable cause', it is the general meeting which can judge whether the cause is reasonable or not and in the absence of fraud the Court will not interfere with the decision of the general meeting.

2.Removal by the Tribunal (Sec.242): According to Section 242 of the Companies Act, 2013 the Tribunal is empowered to remove the director of a company on application made under Section 241 for relief of cases of oppression, mismanagement etc.

If the members of shareholders file a petition under Section 241 before the Tribunal complaining mismanagement and oppression in the company and the Tribunal deems it necessary to provide relief

to the petitioners it may set-aside any agreement or contract which the managing director, director or manager has made with the company and if necessary, may even order removal of the guilty director/manager. The director/manager so removed by the Tribunal, cannot be appointed as managing director, director or manager in any company until the expiry of a period of five years without the consent of Tribunal nor can he claim damages for loss of office i.e. directorship from the company.

Lecture–XII

COMPANY MEETINGS

Chapter XII containing Sections 173 to 195 of Companies Act, 2013, lays down the provisions relating to meetings of the Board of Directors.

The term 'meeting' denotes 'discussions or deliberations on any topic or subject matter by participation/interaction of several/ different minds.' A Company, being an artificial person, cannot act independently. It can act only through the agency of two principal organs, namely:

1. The Board of Directors; and
2. The Shareholders.

The management of the company is vested in a body called 'Board of Directors'. The Board of Directors with the consent of the shareholders act collectively for growth and progress of the company in general and the shareholders in particular.

Important decisions as to the policy matters etc. are taken by the Board of Directors, by passing resolutions in the meetings.

Sections 173 to 176 of the Companies Act, 2013 (Corresponding to Sections 285 to 290) lay down the provisions relating to "meetings of board".

The Companies Act 2013 recognizes four kinds of meetings as stated below –

1. Board of Directors' Meetings.
2. Shareholders' Meetings.
3. Creditors' Meetings, and
4. Debenture Holders' Meetings.

1. Meetings' of the Board (Sec.173): According to Section 173 of the Companies Act, 2013 (Corresponding to Section 285 of the Companies Act, 1956), every company, after its incorporation, shall hold the first meeting of its Board of Directors within thirty days from the date of incorporation and thereafter four meetings in

every calendar year i.e. once in three months. The four meetings shall be held in such a manner that not more than 120 days shall intervene between the two consecutive meetings.

Section 173 runs as follows –

Meetings of Board— (*1*) Every company shall hold the first meeting of the Board of Directors within thirty days of the date of its incorporation and thereafter hold a minimum number of four meetings of its Board of Directors every year in such a manner that not more than one hundred and twenty days shall intervene between two consecutive meetings of the Board:

Provided that the Central Government may, by notification, direct that the provisions of this sub-section shall not apply in relation to any class or description of companies or shall apply subject to such exceptions, modifications or conditions as may be specified in the notification.

(*2*) The participation of directors in a meeting of the Board may be either in person or through video conferencing or other audio visual means, as may be prescribed, which are capable of recording and recognising the participation of the directors and of recording and storing the proceedings of such meetings along with date and time:

Provided that the Central Government may, by notification, specify such matters which shall not be dealt with in a meeting through video conferencing or other audio visual means.

[Provided further that where there is quorum in a meeting through physical presence of directors, any other director may participate through video conferencing or other audio visual means in such meeting on any matter specified under the first proviso]

(*3*) A meeting of the Board shall be called by giving not less than seven days' notice in writing to every director at his address registered with the company and such notice shall be sent by hand delivery or by post or by electronic means:

Provided that a meeting of the Board may be called at shorter notice to transact urgent business subject to the condition that at least one independent director, if any, shall be present at the meeting:

Provided further that in case of absence of independent directors from such a meeting of the Board, decisions taken at such

a meeting shall be circulated to all the directors and shall be final only on ratification thereof by at least one independent director, if any.

(*4*) Every officer of the company whose duty is to give notice under this section and who fails to do so shall be liable to a penalty of twenty-five thousand rupees.

(5) A One Person Company, small company and dormant company shall be deemed to have complied with the provisions of this section if at least one meeting of the Board of Directors has been conducted in each half of a calendar year and the gap between the two meetings is not less than ninety days:

Provided that nothing contained in this sub-section and in section 174 shall apply to One Person Company in which there is only one director on its Board of Directors.

Notice of Meeting: A meeting of the Board of Directors shall be called by giving not less than seven days' notice in writing to every directors at his/her address registered with the company and such notice shall be by hand delivery or by post or by electronic means. However, a shorter notice can be provided to transact urgent business.

Quorum for Meeting of Board (Sec.174): Section 174 of the Companies Act 2013 (Corresponding to Section 287 of the Companies Act, 1956) provides for the quorum for meetings of Board. It runs as follows –

Quorum for meetings of Board— (1) The quorum for a meeting of the Board of Directors of a company shall be one-third of its total strength or two directors, whichever is higher, and the participation of the directors by video conferencing or by other audio visual means shall also be counted for the purposes of quorum under this sub-section.

(2) The continuing directors may act notwithstanding any vacancy in the Board; but, if and so long as their number is reduced below the quorum fixed by the Act for a meeting of the Board, the continuing directors or director may act for the purpose of increasing

the number of directors to that fixed for the quorum, or of summoning a general meeting of the company and for no other purpose.

(3) Where at any time the number of interested directors exceeds or is equal to two-thirds of the total strength of the Board of Directors, the number of directors who are not interested directors and present at the meeting, being not less than two, shall be the quorum during such time.

Explanation: For the purposes of this sub-section, "interested director" means a director within the meaning of sub-section (2) of section 184.

(4) Where a meeting of the Board could not be held for want of quorum, then, unless the articles of the company otherwise provide, the meeting shall automatically stand adjourned to the same day at the same time and place in the next week or if that day is a national holiday, till the next succeeding day, which is not a national holiday, at the same time and place.

Explanation: For the purposes of this section:

(i) any fraction of a number shall be rounded off as one;

(ii) "total strength" shall not include directors whose places are vacant.

Adjournment for want/lack of quorum (Sec.174(4)): Section 174(4) lays down the procedure for adjournment of meeting for want of quorum. If a meeting of the Board could not be held for want of quorum then, unless the articles otherwise provide, the meeting shall automatically stand adjourned till the same day in the next week, at the same time and place. If that day in the next week is a public holiday then the adjournment of the meeting will be till the next succeeding day, which is not a public holiday, at the same time and place.

Passing of Resolution by circulation (Sec.175): The business of the Board is to be transacted by resolutions. Such resolution may be passed either at the meeting of the Board or through circulation. A resolution shall be deemed to have been duly passed by the Board or by a committee thereof by circulation, if the resolution

has been circulated in draft, together with necessary papers, if any, to all the directors or to all the members of the committee, and has been approved by a majority of them who are entitled to vote on the resolution.

Section 175 runs as follows:

Passing of resolution by circulation— (1) No resolution shall be deemed to have been duly passed by the Board or by a committee thereof by circulation, unless the resolution has been circulated in draft, together with the necessary papers, if any, to all the directors, or members of the committee, as the case may be, at their addresses registered with the company in India by hand delivery or by post or by courier, or through such electronic means as may be prescribed and has been approved by a majority of the directors or members, who are entitled to vote on the resolution:

Provided that, where not less than one-third of the total number of directors of the company for the time being require that any resolution under circulation must be decided at a meeting, the chairperson shall put the resolution to be decided at a meeting of the Board.

(2) A resolution under sub-section (1) shall be noted at a subsequent meeting of the Board or the committee thereof, as the case may be, and made part of the minutes of such meeting.

Proceedings of Board's Meeting: The procedure and the mode of conduct of the business in the Board's meeting are usually contained in the articles of the company. The Regulations contained in Schedule I of the Companies Act, 2013 provide that decisions in the Board's meeting shall be taken by majority of votes. But in the absence of such a provision, the chairman does not have a casting vote. Matters to be decided in the Board's meeting are put in the form of resolutions which should be proposed, seconded and duly approved. The resolution may be passed either at the meeting or by circulation. No resolution shall be deemed to have been passed by the Board of a committee thereof, by circulation, unless it has been circulated in draft, together with the necessary papers, if any, to all the directors, or all the members of the committee, as the case

may be, and has been approved by them. Once a resolution is passed in the Board's meeting, it is binding on all the directors whether they voted for or against it.

Minutes (Sec.118): The proceedings of Board's meeting or any of its committees meeting are recorded in a minute-book kept for the purpose. The entries relating to the proceedings of the meeting must be entered in the minute book within thirty days of the conclusion of such meeting. The pages of the minute book should be consecutively numbered. The chairman of the Board must put his initials or signatures on each and every page of the minute book as also in the end.

The minutes of the meeting kept in accordance with the provision stated above, shall be evidence of the proceedings recorded therein. The purpose of the Minute Book is to enable the shareholders of the company 'to know exactly what their directors have been doing, why it was done, and when it was done'.

Any default on the part of company in complying with the provisions of this section (i.e. Sec.118) in respect of any meeting, the company shall be liable to a penalty of twenty-five thousand rupees and every officer of the company who is in default shall be liable to a penalty of five thousand rupees.

Where a person is found guilty of tampering with the minutes of the proceedings of meeting, he shall be punishable with imprisonment for a term which may extend to two years and with fine which shall not be less than twenty-five thousand rupees which may extend to one lakh rupees.

Where the meeting of Board was held under order of High Court directing a person to preside the meeting, the minutes recorded by such person n dot by Company Secretary should be accepted as authentic, more over when there was conflict between two groups and the Court had found a via-media by appointing third agreeable person.

Validity of acts of Directors (Sec. 176): According to Section 176 of the Companies Act, 2013 (Corresponding to Section 290 of the Companies Act, 1956), acts done by a person, as a

director shall be valid, notwithstanding that it may afterwards be discovered that his appointment was invalid by reason of any defect or disqualification or had terminated by virtue of any provision contained in this Act or in the articles. However, if the act of a director has been done after his appointment has been shown to the company to be invalid or to terminate, such an act would be invalid.

Section 176 runs as follows:

No act done by a person as a director shall be deemed to be invalid, notwithstanding that it was subsequently noticed that his appointment was invalid by reason of any defect or disqualification or had terminated by virtue of any provision contained in this Act or in the articles of the Company:

Provided that nothing in this section shall be deemed to give validity to any act done by a director after his appointment has been noticed by the company to be invalid or to have terminated.

2. Share holders' Meeting

According to Companies Act, 2013, there are two kinds of Shareholders' Meetings, namely:—

1. Annual General Meeting (Sec.166 to 168); and

2. Extra-ordinary General Meeting (Sec.169).

1. Annual General Meeting (Sec.96): According to Section 96 of the Companies Act, 2013, (Corresponding to Section 166 of the Companies Act, 1956) every company other than a One Person Company shall hold at least one meeting of its share holders, in addition to any other meetings/meetings in each/calendar year. This meeting is known as 'Annual General Meeting'. The first meeting must be held within nine months from the date of closing of the first financial year of the company. In other cases, the annual general meeting shall be held within a period of six months from the closing of the financial year. The gap between two meetings should not exceed 15 months. The purpose of this meeting is to protect the interests of the shareholders.

In view of Section 96(2) it is mandatory to call the annual general meeting in business hours between 6 a.m. to 6 p.m. on any day that is not a National Holiday.

Ordinarily, annual general meeting shall be called at place wherein the registered office of the company is situated or at some place within city, town or village in which registered office of the company is located.

However, the Central Government is empowered to exempt any company from aforesaid provision.

By virtue of Section 97 the Tribunal is empowered to call annual general meeting.

The Registrar can, for any special reason, extend the time within which any annual general meeting is required to be held by a period not exceeding 3 months but the time for holding the first annual general meeting cannot be so extended.

The penalty for non-holding of annual general meeting can be imposed upon the company as well as every officer, who is in default. For illustration —

In ***Shri Meenakshi Mills Co. v. Assistant Registrar of Joint Stock Companies,*** **AIR 1938 Mad. 640,** a meeting was called in December, 1934 but it was adjourned in March, 1935 and then held. The next meeting was held in February 1936. The company was convicted for not holding an annual general meeting in 1935. The meeting held in March 1935 was the adjourned meeting of 1934.

An annual meeting may be called by giving not less than 21 days' notice in writing. However, notice of less than 21 days served on a shareholder will not invalidate the meeting and the proceedings at the meeting. Besides, an annual meeting may be called with a shorter notice if it is agreed by all the members entitled to vote in the meeting. Every annual general meeting must be called for at any time during business hours on a day that is not a public holiday.

Consequences for not holding the meeting: If a company fails to hold the annual general meeting, two consequences will follow:

Firstly, any member may apply to the Tribunal for directing the company to call the meeting. The Tribunal can give any ancillary directions to the company which is deems expedient for calling the meeting. This power has been exceedingly conferred on the Tribunal by Section 97(2) of the Act and the Tribunal cannot exercise it even under its inherent powers.

Secondly, failure to call the annual general meeting by the company or in pursuance of the order of the Tribunal is an offence punishable with fines which may extend to one lakh rupees and in case of continuing default, with a further fine which may extend to five thousand five hundred rupees for every day until the default continues. This provision is applicable to public as well as private companies.

In *Bejoy Kumar Karnani v. Asst. Registrar of Companies* (1985) 58 Comp. Cas. 293 Cal.), the Calcutta High Court held that as provided in Section 166(1) of the Companies Act, 1956 (now Section 96 of the Companies Act, 2013) in no case the interval between the two consecutive annual general meetings of a company should exceed the statutory limit of fifteen months. The Registrar can extend the period upto three months for such as meeting provided it is not the first annual general meeting. The meeting must be brought to completion within the period of fifteen months notwithstanding adjournments.

But in *KastoormalBanthiya v. State* (AIR 1951 Ajmer 39), where the accused and his brother were the only two members and directors of a private company and during the period when a meeting should have been held, his brother was lying seriously ill. The failure to hold the meeting was not considered to be willful default as there was valid reason for the delay.

Importance: It is the annual meeting at which the shareholders can exercise control over the affairs of the company. At this meeting some directors retire and come up for re-election and thereby the shareholders find an opportunity to refuse to re-elect a director of whose action and policy they disapprove. Appointment of Auditors is also made at this meeting.

Annual accounts are presented at this meeting for the consideration of the shareholders and the shareholders can ask any question relating to the accounts. It is at this meeting that dividends are declared. At this meeting the shareholders can discuss any other matters relating to the company's business.

3. Extra-ordinary General Meeting (Sec. 100): Section 100 of the Companies Act, 2013 (Corresponding to Section 169 of the Companies Act, 1956) provides for calling of extra ordinary general meeting. The Annual general meeting is also known as 'Ordinary Meeting', and a meeting other than the Annual General Meeting is called 'Extra-ordinary General Meeting'. It is called for transacting some urgent or special business, which cannot be postponed/awaited till the next annual general meeting. It is convened/held on the requisition of the members having at least 1/10th paid up capital (in the absence of capital, 1/10th voting power). It is convened

1. by the Board of directors on its own or on the requisition of the members; or
2. by the requisitionists themselves on the failure of the Board of directors to call the meeting.

1. By the Board of Directors: The Board of Directors can call such a meeting whenever it deems fit (i.e. the Board may call on its own motion). But they must call an extraordinary meeting on the requisition of –

(i) in the case of a company having a share capital, by the holders of at least one-tenth paid-up capital having the right to vote on the matter of requisition;

(ii) in the case of a company not having a share capital, by members representing not less than one-tenth of the total voting power in regard to the matter of requisition.

When a requisition is deposited at the registered office of a company, the meeting must be held within 45 days from the date of the requisition.

2. By the requisitionists: If the directors do not call an extraordinary meeting as required by the requisition in the manner stated above, the requisitionists may themselves proceed to call the meeting and recover the necessary expenses from the company.

The Apex Court in *Life Insurance Corporation Ltd. v. Escorts Ltd.* (AIR 1986 SC 1370), held that every share holder of a company has the right, subject to statutorily prescribed procedure and numerical requirements to call an extraordinary general meeting in accordance with the provisions of the Companies Act, he cannot be restricted from calling a meeting and he is not bound to disclose the reasons for the resolution proposed to be moved at the meeting. Nor are the reasons for the resolutions subject to the judicial scrutiny.

Power of Tribunal to order/call extra ordinary General Meeting (Sec. 98): Section 98 of the Companies Act, 2013 (Corresponding to Section 186 of the Companies Act, 1956) confers the Tribunal, power to order/call for extra ordinary general meeting. It runs as follows –

Power of Tribunal to call meetings of members, etc— (1) If for any reason it is impracticable to call a meeting of a company, other than an annual general meeting, in any manner in which meetings of the company may be called, or to hold or conduct the meeting of the company in the manner prescribed by this Act or the articles of the company, the Tribunal may, either *suo motu* or on the application of any director or member of the company who would be entitled to vote at the meeting:

(a) order a meeting of the company to be called, held and conducted in such manner as the Tribunal thinks fit; and

(b) give such ancillary or consequential directions as the Tribunal thinks expedient, including directions modifying or supplementing in relation to the calling, holding and conducting of the meeting, the operation of the provisions of this Act or articles of the company:

Provided that such directions may include a direction that one member of the company present in person or by proxy shall be deemed to constitute a meeting.

(2) Any meeting called, held and conducted in accordance with any order made under sub-section (1) shall, for all purposes, be deemed to be a meeting of the company duly called, held and conducted.

If for any reason it is impracticable to call extraordinary general meeting, the Tribunal on an application or *suomotu* may call such meeting other than the annual general meeting. An extraordinary meeting called by order of the Tribunal shall be deemed to be a meeting for all purposes.

Resolutions (Sections 114 and 115)

Section 114 and 115 of the Companies Act, 2013 (Corresponding to Sections 189 and 190 respectively of the Companies Act, 1956) prescribe the procedure for recording the decisions taken in the meetings by passing resolutions of the company.

In the meetings, decisions taken are recorded by means of resolutions with the provisions relating to the resolutions. The resolutions are of three kinds, namely —

1. Ordinary Resolution (Sec.114(1).
2. Special Resolution (Sec.114(2) and
3. Resolutions requiring special notice (Sec.115).

1. Ordinary Resolution (Sec. 114(1): It is passed at General Meeting by simple majority (including casting vote of the chairman and proxies). Proxy is a person appointed or deputed by a member, to participate and vote on his behalf in the meeting.

E.g.: In a general meeting of a company, out of 1000 members entitled to vote, only 700 are present. Of these 700, 251 members vote in favour of a resolution, 250 against it, and 199 abstain from voting. The resolution is passed by a simple majority.

When is an ordinary resolution required? Ordinary resolution is necessary for the following among other purposes:

a) To rectification of name or adoption of new name by a company where it resembles the name of an existing company (Sec.16).

b) To vary terms and conditions in the prospectus/statement in lieu of prospectus (Sec.27).

c) Issue of shares at a discount (Sec.53).

d) Alternation of share capital (Sec.61).

e) To declare dividend (Sec.123).

f) To approve annual accounts and balance sheet (Sec.129.

g) To appointment of first directors who are liable to retire by rotation (Sec.152).

h) To appoint directors (Sec.152).

i) To appoint a person who is not retiring director (Sec.160).

j) To remove a director and appoint another director in his place (Sec.169).

k) To give consent for the exercise of power by the Board (Sec.180).

l) To approve appointment of sole selling agents (Sec.188).

m) To approve voluntary winding up if the articles provided (Sec.304).

n) To approve appointment and remuneration of liquidator for voluntary winding up (Sec.310).

o) To authorize the Board of Directors to exercise certain powers after appointment of Liquidator (Sec.313).

p) To fill up the vacancy in the office of Liquidator (Sec.311).

q) To consider accounts prepared by the Liquidator in voluntary winding up (Sec.316).

r) To nominate creditors' representative as Liquidator in voluntary winding up (Sec.310).

s) To appoint a committee of inspection in creditors' voluntary winding up (Sec.315).

t) To consider accounts prepared by the Liquidator in creditor's voluntary winding up (Secs.316-318).

2. Special Resolution (Sec.114(2): It is possessed in the General Meeting by 3/4th majority (including proxies allowed).

Section 114(2) of the Companies Act, 2013 defines 'Special Resolution'. A resolution is special when intention to proposed resolution as 'Special Resolution' has been duly specified in the notice called meeting or any other intimation about such resolution has been given to the members of the company.

The Supreme Court in *M.S.Madhusudhanan v. Kerala Kaumudi Pvt.Ltd.* (AIR 2004 SC 909 (926), held that notice of Special Resolution under Section 189(2)(a) of the Companies Act, 1956, (now Section 114(2) of the Companies Act, 2013) should be sufficiently specific so as to effectively inform each member the actual resolution sought to be passed in the general meeting. The notice must be frank, open, clear and satisfactory. If it is not so, the notice is bad in law and the special resolution shall stand vitiated and cannot be accepted upon. This case involved a special resolution sought to be passed by the Company in its general meeting for alteration in its Articles of Association. Held, the notice for resolution was not sufficiently clear and therefore was bad in law.

The Court further made it clear that three conditions must be fulfilled before any alteration of the Articles of Association could take place –

i) The notice must clearly specify the intention to propose the resolution as an extraordinary resolution.

ii) The resolution must be passed by three times the number of votes cast against the resolution by members (share holders) so entitled to vote.

iii) Not less than 21 days notice on the meeting must have been given.

Special Resolution is necessary in the following matters:

a) To alter the provisions of the memorandum so as to change the place of registered office from one State to another, or to change the objects of the company (confirmation by the Company Law Board is also necessary (Sec.13).

b) To remove the registered office of the company outside the local limits of the city, town or village in which situated (Sec.12).

c) To change the name of the company with the approval of the Central Government (Sec.13).

d) To alter or add to the articles of association (Sec.14).

e) To change the name by omitting 'Limited' or 'Private Limited' with the permission of the Central Government (Sec.8(1).

f) To reduce the share capital with the permission of the Tribunal (Sec.66(1).

g) To make variations in the rights of special classes of shares (Sec.48).

h) To declare that the company's affairs ought to be investigated by an inspector appointed by the Central Government (Sec.213).

i) To determine the remuneration payable to any director including managing director (Sec.197).

j) To obtain an order from the Court for the winding up of a company (Sec.271).

k) To wind up the company voluntarily (Sec.304).

l) To confer general authority on the liquidator or an authority in respect of any particular arrangement with reference to the proposed sale of property of company in voluntary liquidation (Sec.319).

m) To enable the liquidator in member's voluntary winding up to exercise certain powers (Secs.314 and 343).

n) To make binding on company and creditors any arrangement entered into between a company, about to be or in course of being wound up and its creditors (Sec.321).

o) To direct the matter of disposing of a company's books and papers on the completion of a members' voluntary winding up (Sec.347).

p) To render possible the application of Table F of Schedule I to a company registered under Part IX to the extent as it is adopted by the special resolution (Sec.371).

q) To issue further shares to any persons other than equity share holders (Sec.62).

r) To keep Register of Members at a place other than the registered office (Sec.94).

The object of requiring a majority of 3/4th of the votes for a special resolution is to protect the minority interests in important matters relating to the company's affairs.

When is a special resolution required? Special resolution is necessary for the following among other purposes:

a) Alteration of Memorandum for changing the place of registered office from one State to another with the leave of the Central Government [Sec.13]. Special resolution is also required for changing the 'objects clause' of the Memorandum.

b) Change of name of a company with the consent of the Central Government.

c) Omission or addition of the word 'Private' from, or to, the name of a compant.

d) Change of name of a charitable or other non-profit company by omitting the word or words 'Limited' or 'Private Limited' [Sec.8(1)].

e) Alteration of the Articles of a company [Sec.14].

f) Reduction of share capital [Sec.66].

g) Variation of shareholders' rights [Sec.48].

h) Removal of a company's registered office outside the local limits of any city, town or village [Sec.12].

i) Keeping registers and returns at a place other than the registered office [Sec.94].

j) Applying to the Central Government for appointing as Inspector for investigating a company's affairs in some cases [Sec.213].

k) Fixing the remuneration of all managerial personnel in the abuse or inadequacy of profits where the Articles require such resolution [Sec.197].

l) Applying to the Tribunal to wind up a company [Sec.271].

m) Winding up a company voluntarily [Sec.304].

n) Authorising the liquidator of a company to accept shares as consideration for the transfer of its assets [Sec.319].

o) Disposal of books and papers of a company in voluntary winding up when its affairs have been completely wound up [Sec.347].

The Companies Act requires sanction of shareholders by a special resolution in respect of a number of matters (in addition to those given above) dealt with in Sections 62, 12, 11, 321 and 343.

3. Resolutions requiring Special Notice (Sec.115): Section 115 of the Companies Act, 2013 (Corresponding to Section 190 of the Companies Act, 1956) deals with resolutions requiring special notice. It runs as follows –

Where, by any provision contained in this Act or in the articles of a company, special notice is required of any resolution, notice of the intention to move such resolution shall be given to the company by such number of members holding not less than one per cent of total voting power or holding shares on which such aggregate sum not exceeding five lakh rupees, as may be prescribed, has been paid up and the company shall give its members notice of the resolution in such manner as may be prescribed.

Where, by the provisions of the Companies Act or in the articles, special notice of any resolution is required, a notice of the intention to move the resolution must be given at least 14 days before the meeting. Under the Companies Act a special notice is required for the removal of an auditor other than the retiring auditor [Sec.140], or when it is expressly provided that the retiring auditor shall not be re-appointed, or the removal of a director or for the appointment of a director in place of a director who has been removed [Sec.169].

After the company has received the special notice of the resolution, in its own turn, should give the notice of the resolution to its members in the same manner as it gives the notice of the meeting, or if that is not practicable then by advertisement in the newspaper having an appropriate circulation or in any other mode allowed by the articles, at least 7 days before the meeting [Sec.115].

Cases in respect of which resolutions by special notice is required: The Companies Act, 2013 requires special notice for passing resolutions in the following cases –

a) For resolution at an annual general meeting to provide expressly that the retiring auditor will not be reappointed (Sec.140).

b) For a resolution at an annual general meeting appointing an auditor, a person other than a retiring auditor (Sec.140).

c) For a resolution to remove a director before the expiry of his period of office (Sec.169).

d) For a resolution to appoint another director in place of the so removed director (Sec.284).

e) Where the articles of a company provide for the giving of a special notice for a resolution, in respect of any matter or matters.

Proxy (Sec. 105)

Section 105 of the Companies Act, 2013 (Corresponding to Section 176 of the Companies Act, 1956) lays down the provision relating to 'Proxies'. It runs as follows:

Proxies— (1) Any member of a company entitled to attend and vote at a meeting of the company shall be entitled to appoint another person as a proxy to attend and vote at the meeting on his behalf:

Provided that a proxy shall not have the right to speak at such meeting and shall not be entitled to vote except on a poll:

Provided further that, unless the articles of a company otherwise provide, this sub-section shall not apply in the case of a company not having a share capital:

[3]Provided also that the Central Government may prescribe a class or classes of companies whose members shall not be entitled to appoint another person as a proxy:

[3]Provided also that a person appointed as proxy shall act on behalf of such member or number of members not exceeding fifty and such number of shares as may be prescribed.

(2) In every notice calling a meeting of a company which has a share capital, or the articles of which provide for voting by proxy at the meeting, there shall appear with reasonable prominence a statement that a member entitled to attend and vote is entitled to appoint a proxy, or, where that is allowed, one or more proxies, to attend and vote instead of himself, and that a proxy need not be a member.

(3) If default is made in complying with sub-section (2), every officer of the company who is in default shall be punishable with fine which may extend to five thousand rupees.

(4) Any provision contained in the articles of a company which specifies or requires a longer period than forty-eight hours before a meeting of the company, for depositing with the company or any other person any instrument appointing a proxy or any other document necessary to show the validity or otherwise relating to the appointment of a proxy in order that the appointment may be effective at such meeting, shall have effect as if a period of forty-eight hours had been specified in or required by such provision for such deposit.

(5) If for the purpose of any meeting of a company, invitations to appoint as proxy a person or one of a number of persons specified in the invitations are issued at the company's expense to any member entitled to have a notice of the meeting sent to him and to vote thereat by proxy, every officer of the company who knowingly issues the invitations as aforesaid or wilfully authorises or permits their issue shall be punishable with fine which may extend to one lakh rupees:

Provided that an officer shall not be punishable under this sub-section by reason only of the issue to a member at his request in writing of a form of appointment naming the proxy, or of a list of

persons willing to act as proxies, if the form or list is available on request in writing to every member entitled to vote at the meeting by proxy.

(6) The instrument appointing a proxy shall:

(a) be in writing; and

(b) be signed by the appointer or his attorney duly authorised in writing or, if the appointer is a body corporate, be under its seal or be signed by an officer or an attorney duly authorised by it.

(7) An instrument appointing a proxy, if in the form as may be prescribed, shall not be questioned on the ground that it fails to comply with any special requirements specified for such instrument by the articles of a company.

(8) Every member entitled to vote at a meeting of the company, or on any resolution to be moved thereat, shall be entitled during the period beginning twenty-four hours before the time fixed for the commencement of the meeting and ending with the conclusion of the meeting, to inspect the proxies lodged, at any time during the business hours of the company, provided not less than three days' notice in writing of the intention so to inspect is given to the company.

The word 'Proxy' literally means "the authority conferred to act on behalf of another." The term 'proxy' has a double meaning. A member entitled to attend and vote at a meeting may vote either in person or by proxy. A proxy is an authority to represent and vote for another person at a meeting. It is also an instrument appointing a person as proxy. The person so appointed is also called a proxy. A proxy is not entitled to act contrary to the instructions of the appointer. The proxy may or may not be a member of the company but he shall not have any right to speak at the meeting.

Prior to the Companies Act, 1956 a member had no statutory right to vote by proxy but the articles of companies usually provided that a member could appoint another member of the company as his proxy, but such a proxy had no right to demand a poll at the meeting. However, Section 105 of the Companies Act, 2013

provides that any member entitled to attend and vote at a meeting is entitled to appoint another person whether a member or not, as his proxy to attend and vote on his behalf, but a proxy so appointed shall not have any right to speak, at the meeting.

Instrument : Appointing Proxy (Sec.105(6)): According to this section the instrument appointing a proxy shall be in writing and be signed by the appointer or his/her attorney duly authorized in writing if an appointer is a body corporate it be under its seal or be signed by an officer or any attorney duly authorized by it.

Voting by show of hands (Sec. 107): Unless a poll is demanded (i.e. Sec.109) or the voting is carried out electronically, at any general meeting, a resolution put to vote of the meeting, it shall be decided on a show of hands.

However, if a resolution passed or rejected by the show of hands is entered in the minutes of meeting it shall be regarded as a conclusive evidence of the fact of passing/rejecting resolution.

Voting through electronic means (Sec.108): Now electronic means of voting in a company's meetings including the Board of Director's meeting have been recognized. According to Section 108 of the Companies Act, 2013 the Central Government may prescribe the class or classes of companies and manner in which a member may exercise his/her right to vote by the electronic means.

Postal Ballot (Sec.110): A company with prior approval of the Central Government and by notification to this effect, such terms of business are declared to be transacted only by means of postal ballot.

A member of a private company cannot appoint more than one proxy for the same occasion. A proxy is not entitled to vote except on poll.

Process:

1. The instrument of proxy must be in accordance with the Provisions of the Companies Act, 2013.

2. It must be in writing and signed by the Appointer or his attorney and duly stamped according to Stamps Act.

3. Every member is entitled to examine/inspect the proxies, 24 hours before the meeting. For this purpose, 3 days' time is given.

4. The relationship of Appointer and proxy is that of the principal and Agent.

5. The instrument of proxy must be deposited 48 hours before the meeting.

Section 105 of the Act contains provisions relating to proxies which are as follows:

1. Any member of a company who is entitled to attend and vote at a meeting of the company has a statutory right to appoint another person (whether a member or not) as a proxy to vote ad attend in his place. But he has no right to speak. However, he cannot vote on a show of hands. A member of a private company shall not be entitled to appoint more than one proxy to attend on the same occasion.

2. Every notice of a general meeting must state with reasonable prominence that a member entitled to attend and vote is entitled to appoint a proxy to attend and vote instead of him and that a proxy need not be a member. Any default in not complying with this provision shall make the officer in default liable to be punished with fine which may extend to five thousand rupees.

3. The instrument appointing a proxy must be in writing and signed by the shareholders. It should be deposited with the company forty eight house before the meeting. Proxy forms should be supplied to the members along with the notice of the meeting. The forms should be blank ad carry no suggestion to influence the voting in any way.

4. A proxy is revocable subject to the provisions of the articles. But revocation must naturally be received in the office of the company before the commencement of the meeting. In *K.P.Chackocham v. Federal Bank* (1989) 66 Comp Cas 953 (Ker), a proxy received

before the poll, but after the meeting had commenced, was held to be ineffective and the proxy's vote was not counted. However, in absence of any provision to this effect in the articles, the power of revocation would be unfettered and it can well be revoked sandy time before the final poll is held.

5. Every member who is entitled to vote at a meeting of the Company is entitled to inspect the proxy forms during the period beginning twenty four house hours before the time of commencement of the meeting and ending with the conclusion of the meeting provided not less than three days prior notice in writing is given to the company. Such inspection cannot be made by proxy himself.

6. As provided under Section 105 of the Companies Act, 2013, a person appointed as proxy shall act on behalf of such number of members not exceeding 50 and such number of shares as may be prescribed. There was no such provision in the earlier Companies Act, 1956.

The above provisions of the Act relating to proxies do not apply to a company not having a share capital; and also to a private company which is not a subsidiary of a public company, if such private company otherwise provides in its articles.

Section 105 of the Companies Act, 2013 also provides that the Central Government may prescribe or classes of companies whose members shall not be entitled to appoint proxies. There was no such provision in the preceding Companies Act, 1956.

3. Creditors' Meeting

The Creditors' meeting is convened where a compromise or arrangement is proposed between a company and its creditors. The (Tribunal) may, on the application of the company or of any creditor or member of the company, in case of a company being wound up, even on the liquidator's application may call meeting by order, to be held and conducted in such manner as the (Tribunal) directs. However, the meeting of creditors may be convened for the following purposes –

i) To enter into an arrangement or a compromise between a company and creditors or any class of them, or for an arrangement or a compromise between a company and its members or any class of them.

ii) To seek approval of creditors for amalgamation or reconstruction of a company, or

iii) To seek consent of the creditors for winding up of a company.

Where the company is being wound up, any creditor or class of creditors or liquidator may apply to the Tribunal for ordering a meeting of the creditors or class of creditors.

According to Section 509(2)(b) of the Companies Act, 1956 each creditors' meeting shall be called by advertisement published not less than one month before the meeting in the Official Gazette and also in some newspapers circulating in the district where the registered office of the company is situated.

4. Debenture-holders' Meeting

The company may call the debenture holders' meeting for the following purposes –

a) Any variation in the conditions of their security, or

b) Any alternation in their rights, or

c) Effecting change in rate of interest on the existing debentures, or

d) For issuing of new debentures.

Registration of resolutions: In accordance with Section 192(4) of the Companies Act, 1956 (Corresponding Section 117(1) of the Companies Act, 2013) the following resolutions are required to be registered with the Registrar of Companies:

i) Special resolution.

ii) Resolutions which have been agreed to by all the members of a company, but which, in the absence of such an agreement would have to be passed as special resolutions.

iii) Any resolution of the Board of Directors of a company or agreement executed by a company, relating to the appointment, re-appointment or renewal of the appointment, or variation of the terms of appointment, of a managing director.

iv) Resolution regarding a company to be wound up voluntarily.

v) Resolution passed by a company conferring power under Section 180 upon its directors:

— to sell or dispose of the whole or any part of the company's undertaking, or

— to borrow money beyond the limits of the paid up capital free reserves and securities premium of the company, or

— to contribute to charities beyond fifty thousand rupees or five per cent of its net profits in any financial year, whichever is greater.

Such resolutions or agreements must be filed with the Registrar of Companies within 30 days from the date of resolutions passed or agreement entered into; the copy to be filed must be certified under the signature of an officer of the company.

Lecture – XIII
ACCOUNTS OF COMPANIES

Chapter IX containing Sections 128 to 138 of the Companies Act, 2013 lays down the provisions relation to maintenance of the Accounts of Companies as detailed below –

Books of account etc. to be kept by Company (Sec.128):

(1) Every company shall prepare and keep at its registered office books of account and other relevant books and papers and financial statement for every financial year which give a true and fair view of the state of the affairs of the company, including that of its branch office or offices, if any, and explain the transactions effected both at the registered office and its branches and such books shall be kept on accrual basis and according to the double entry system of accounting:

Provided that all or any of the books of account aforesaid and other relevant papers may be kept at such other place in India as the Board of Directors may decide and where such a decision is taken, the company shall, within seven days thereof, file with the Registrar a notice in writing giving the full address of that other place:

Provided further that the company may keep such books of account or other relevant papers in electronic mode in such manner as may be prescribed.

(2) Where a company has a branch office in India or outside India, it shall be deemed to have complied with the provisions of sub-section (*1*), if proper books of account relating to the transactions effected at the branch office are kept at that office and proper summarised returns periodically are sent by the branch office to the company at its registered office or the other place referred to in sub-section (1).

(3) The books of account and other books and papers maintained by the company within India shall be open for inspection at the registered office of the company or at such other place in India by any director during business hours, and in the case of financial

information, if any, maintained outside the country, copies of such financial information shall be maintained and produced for inspection by any director subject to such conditions as may be prescribed:

Provided that the inspection in respect of any subsidiary of the company shall be done only by the person authorised in this behalf by a resolution of the Board of Directors.

(4) Where an inspection is made under sub-section (3), the officers and other employees of the company shall give to the person making such inspection all assistance in connection with the inspection which the company may reasonably be expected to give.

(5) The books of account of every company relating to a period of not less than eight financial years immediately preceding a financial year, or where the company had been in existence for a period less than eight years, in respect of all the preceding years together with the vouchers relevant to any entry in such books of account shall be kept in good order:

Provided that where an investigation has been ordered in respect of the company under Chapter XIV, the Central Government may direct that the books of account may be kept for such longer period as it may deem fit.

(6) If the managing director, the whole-time director in charge of finance, the Chief Financial Officer or any other person of a company charged by the Board with the duty of complying with the provisions of this section, contravenes such provisions, such managing director, whole-time director in charge of finance, Chief Financial Officer or such other person of the company shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees or with both.

Financial statement (Sec. 129)

(1) The financial statements shall give a true and fair view of the state of affairs of the company or companies, comply with the accounting standards notified under section 133 and shall be in the

form or forms as may be provided for different class or classes of companies in Schedule III:

Provided that the items contained in such financial statements shall be in accordance with the accounting standards:

Provided further that nothing contained in this sub-section shall apply to any insurance or banking company or any company engaged in the generation or supply of electricity, or to any other class of company for which a form of financial statement has been specified in or under the Act governing such class of company:

Provided also that the financial statements shall not be treated as not disclosing a true and fair view of the state of affairs of the company, merely by reason of the fact that they do not disclose:

(a) in the case of an insurance company, any matters which are not required to be disclosed by the Insurance Act, 1938 (4 of 1938), or the Insurance Regulatory and Development Authority Act, 1999 (41 of 1999);

(b) in the case of a banking company, any matters which are not required to be disclosed by the Banking Regulation Act, 1949 (10 of 1949);

(c) in the case of a company engaged in the generation or supply of electricity, any matters which are not required to be disclosed by the Electricity Act, 2003 (36 of 2003);

(d) in the case of a company governed by any other law for the time being in force, any matters which are not required to be disclosed by that law.

(2) At every annual general meeting of a company, the Board of Directors of the company shall lay before such meeting financial statements for the financial year.

[(3) Where a company has one or more subsidiaries or associate companies, it shall, in addition to financial statements provided under sub-section (2), prepare a consolidated financial statement of the company and of all the subsidiaries and associate

companies in the same form and manner as that of its own and in accordance with applicable accounting standards, which shall also be laid before the annual general meeting of the company along with the laying of its financial statement under sub-section (2):

Provided that the company shall also attach along with its financial statement, a separate statement containing the salient features of the financial statement of its subsidiary or subsidiaries and associate company or companies in such form as may be prescribed:

Provided further that the Central Government may provide for the consolidation of accounts of companies in such manner as may be prescribed].

(4) The provisions of this Act applicable to the preparation, adoption and audit of the financial statements of a holding company shall, *mutatis mutandis,* apply to the consolidated financial statements referred to in sub-section (3).

(5) Without prejudice to sub-section (1), where the financial statements of a company do not comply with the accounting standards referred to in sub-section (1), the company shall disclose in its financial statements, the deviation from the accounting standards, the reasons for such deviation and the financial effects, if any, arising out of such deviation.

(6) The Central Government may, on its own or on an application by a class or classes of companies, by notification, exempt any class or classes of companies from complying with any of the requirements of this section or the rules made thereunder, if it is considered necessary to grant such exemption in the public interest and any such exemption may be granted either unconditionally or subject to such conditions as may be specified in the notification.

(7) If a company contravenes the provisions of this section, the managing director, the whole-time director in charge of finance, the Chief Financial Officer or any other person charged by the Board with the duty of complying with the requirements of this section and

in the absence of any of the officers mentioned above, all the directors shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.

Explanation: For the purposes of this section, except where the context otherwise requires, any reference to the financial statement shall include any notes annexed to or forming part of such financial statement, giving information required to be given and allowed to be given in the form of such notes under this Act.

General Instructions for preparation of Balance Sheet and Statement of Profit and Loss of Company

(1)Where compliance with the requirements of the Act including Accounting Standards as applicable to the companies require any change in treatment or disclosure including addition, amendment, substitution or deletion in the head or sub-head or any changes, *inter se*, in the financial statements or statements forming part thereof, the same shall be made and the requirements of this Schedule shall stand modified accordingly.

(2)The disclosure requirements specified in this Schedule are in addition to and not in substitution of the disclosure requirements specified in the Accounting Standards prescribed under the Companies Act, 2013. Additional disclosures specified in the Accounting Standards shall be made in the notes to accounts or by way of additional statement unless required to be disclosed on the face of the Financial Statements. Similarly, all other disclosure as required by the companies Act shall be made in the notes to accounts in addition to the requirements set out in this Schedule.

(3) (i) Notes to accounts shall contain information in addition to that presented in the Financial Statements and shall provide where required (a) narrative descriptions or disaggregations of items recognized in those statements; and (b) information about items that do not qualify for recognition in those statements.

(ii) Each item on the face of the Balance Sheet and Statement of Profit and Loss shall be cross-referenced to any related

information in the notes to accounts. In preparing the Financial Statements including in the notes to accordance, a balance shall be maintained between providing excessive detail that may not assist users of financial statements and not providing important information as a result of too much aggregation.

(4)(i) Depending upon the turnover of the company, the figures appearing in the Financial Statements may be rounded off as given below:

Turnover	Rounding off
1. Less than one hundred crore rupees.	To the nearest hundreds, thousands, lakhs or millions, or decimals thereof.
2. One hundred crore rupees or more.	To the nearest lakhs, millions or crores, or decimals thereof.

(ii) Once a unit of measurement is used, it shall be used uniformly in the Financial Statements.

(5) Except in the case of the first Financial Statements laid before the Company (after its incorporation) the corresponding amounts (comparatives) for the immediately preceding reporting period for the items shown in the Financial Statements including notes shall also be given.

(6) For the purpose of this Schedule, the terms used herein shall be as per the applicable Accounting Standards.

Note:- This part of Schedule sets out the minimum requirements for disclosure on the face of the Balance Sheet, and the Statement of Profit and Loss (hereinafter referred to as 'Financial Statements' for the purpose of this Schedule) and Notes. Line items, sub-line items and sub-totals shall be presented as an addition or substitution on the face of the Financial Statements when such presentation is relevant to an understanding of the company's financial position or performance or to cater to industry/sector-specific disclosure requirements or when required for compliance with the amendments to the Companies Act or under the Accounting Standards.

Re-opening of accounts on Court's or Tribunal Orders (Sec.130)

According to Section 2(29)

'Court' means –

(i) the High Court having jurisdiction in relation to the place at which the registered office of the company concerned is situate, except to the extent to which jurisdiction has been conferred on any district court or district courts subordinate to that High Court under sub-clause (ii);

(ii) the district court, in cases where the Central Government has, by notification, empowered any district court to exercise all or any of the jurisdictions conferred upon the High Court, within the scope of its jurisdiction in respect of a company whose registered office is situate in the district;

(iii) the Court of Session having jurisdiction to try any offence under this Act or under any previous company law;

(iv) the Special Court established under section 435;

(v) any Metropolitan Magistrate or a Judicial Magistrate of the First Class having jurisdiction to try any offence under this Act or under any previous company law;

In accordance with Section 130:

(1) A company shall not re-open its books of account and shall not recast its financial statements, unless an application in this regard is made by the Central Government, the Income-tax authorities, the Securities and Exchange Board, any other statutory regulatory body or authority or any person concerned and an order is made by a court of competent jurisdiction or the Tribunal to the effect that:

(i) the relevant earlier accounts were prepared in a fraudulent manner; or

(ii) the affairs of the company were mismanaged during the relevant period, casting a doubt on the reliability of financial statements:

Provided that the court or the Tribunal, as the case may be, shall give notice to the Central Government, the Income-tax authorities, the Securities and Exchange Board or any other statutory

regulatory body or authority concerned [or any other person concerned] and shall take into consideration the representations, if any, made by that Government or the authorities, Securities and Exchange Board or the body or authority concerned [or the other person concerned] before passing any order under this section.

(2) Without prejudice to the provisions contained in this Act the accounts so revised or re-cast under sub-section (1) shall be final.

[(3) No order shall be made under sub-section (1) in respect of re-opening of books of account relating to a period earlier than eight financial years immediately preceding the current financial year:

Provided that where a direction has been issued by the Central Government under the proviso to sub-section (5) of section 128 for keeping of books of account for a period longer than eight years, the books of account may be ordered to be re-opened within such longer period.]

Voluntary revision of financial statements or Board's report (Sec.131)

(1) If it appears to the directors of a company that:

(a) the financial statement of the company; or

(b) the report of the Board,

do not comply with the provisions of section 129 or section 134 they may prepare revised financial statement or a revised report in respect of any of the three preceding financial years after obtaining approval of the Tribunal on an application made by the company in such form and manner as may be prescribed and a copy of the order passed by the Tribunal shall be filed with the Registrar:

Provided that the Tribunal shall give notice to the Central Government and the Income tax authorities and shall take into consideration the representations, if any, made by that Government or the authorities before passing any order under this section:

Provided further that such revised financial statement or report shall not be prepared or filed more than once in a financial year:

Provided also that the detailed reasons for revision of such financial statement or report shall also be disclosed in the Board's

report in the relevant financial year in which such revision is being made.

(2) Where copies of the previous financial statement or report have been sent out to members or delivered to the Registrar or laid before the company in general meeting, the revisions must be confined to:

(a) the correction in respect of which the previous financial statement or report do not comply with the provisions of section 129 or section 134; and

(b) the making of any necessary consequential alternation.

(3) The Central Government may make rules as to the application of the provisions of this Act in relation to revised financial statement or a revised director's report and such rules may, in particular:

(a) make different provisions according to which the previous financial statement or report are replaced or are supplemented by a document indicating the corrections to be made;

(b) make provisions with respect to the functions of the company's auditor in relation to the revised financial statement or report;

(c) require the directors to take such steps as may be prescribed.

Constitution of National Financial Reporting Authority (Sec.132)

(1) The Central Government may, by notification, constitute a National Financial Reporting Authority to provide for matters relating to accounting and auditing standards under this Act.

(1A) The National Financial Reporting Authority shall perform its functions through such divisions as may be prescribed.

(2) Notwithstanding anything contained in any other law for the time being in force, the National Financial Reporting Authority shall:

(a) make recommendations to the Central Government on the formulation and laying down of accounting and auditing policies and standards for adoption by companies or class of companies or their auditors, as the case may be;

(b) monitor and enforce the compliance with accounting standards and auditing standards in such manner as may be prescribed;

(c) oversee the quality of service of the professions associated with ensuring compliance with such standards, and suggest measures required for improvement in quality of service and such other related matters as may be prescribed; and

(d) perform such other functions relating to clauses (a), (b) and (c) as may be prescribed.

(3) The National Financial Reporting Authority shall consist of a chairperson, who shall be a person of eminence and having expertise in accountancy, auditing, finance or law to be appointed by the Central Government and such other members not exceeding fifteen consisting of part-time and full-time members as may be prescribed:

Provided that the terms and conditions and the manner of appointment of the chairperson and members shall be such as may be prescribed:

Provided further that the chairperson and members shall make a declaration to the Central Government in the prescribed form regarding no conflict of interest or lack of independence in respect of his or their appointment:

Provided also that the chairperson and members, who are in full-time employment with National Financial Reporting Authority shall not be associated with any audit firm (including related consultancy firms) during the course of their appointment and two years after ceasing to hold such appointment.

(3A) Each division of the National Financial Reporting Authority shall be presided over by the Chairperson or a full-time Member authorised by the Chairperson.

(3B) There shall be an executive body of the National Financial Reporting Authority consisting of the Chairperson and full-time Members of such Authority for efficient discharge of its functions under sub-section (2) [other than clause (a)] and sub-section (4).

(4) Notwithstanding anything contained in any other law for the time being in force, the National Financial Reporting Authority shall:

(a) have the power to investigate, either *suo motu* or on a reference made to it by the Central Government, for such class of bodies corporate or persons, in such manner as may be prescribed into the matters of professional or other misconduct committed by any member or firm of chartered accountants, registered under the Chartered Accountants Act, 1949 (38 of 1949):

Provided that no other institute or body shall initiate or continue any proceedings in such matters of misconduct where the National Financial Reporting Authority has initiated an investigation under this section;

(b) have the same powers as are vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908), while trying a suit, in respect of the following matters, namely:

(i) discovery and production of books of account and other documents, at such place and at such time as may be specified by the National Financial Reporting Authority;

(ii) summoning and enforcing the attendance of persons and examining them on oath;

(iii) inspection of any books, registers and other documents of any person referred to in clause (b) at any place;

(iv) issuing commissions for examination of witnesses or documents;

(c) where professional or other misconduct is proved, have the power to make order for:

(A) imposing penalty of:

(I) not less than one lakh rupees, but which may extend to five times of the fees received, in case of individuals; and

(II) not less than [five] lakh rupees, but which may extend to ten times of the fees received, in case of firms;

(B) debarring the member or the firm from –

I. being appointed as an auditor or internal auditor or undertaking any audit in respect of financial statements or internal audit of the functions and activities of any company or body corporate; or

II. performing any valuation as provided under section 247,

for a minimum period of six months or such higher period not exceeding ten years as may be determined by the National Financial Reporting Authority.

Explanation: For the purposes of his (Sic this) sub-section, the expression "professional or other misconduct" shall have the same meaning assigned to it under section 22 of the Chartered Accountants Act, 1949 (38 of 1949).

(5) Any person aggrieved by any order of the National Financial Reporting Authority issued under clause (c) of sub-section (4), may prefer an appeal before [the Appellate Tribunal in such manner and on payment of such fee as may be prescribed].

(6) [xxx]

(7) [xxx]

(8) [xxx]

(9) The officer authorised by the Appellate Authority shall prepare in such form and at such time as may be prescribed its annual report giving a full account of its activities and forward a copy thereof to the Central Government and the Central Government shall cause the annual report to be laid before each House of Parliament.

(10) The National Financial Reporting Authority shall meet at such times and places and shall observe such rules of procedure in regard to the transaction of business at its meetings in such manner as may be prescribed.

(11) The Central Government may appoint a secretary and such other employees as it may consider necessary for the efficient performance of functions by the National Financial Reporting Authority under this Act and the terms and conditions of service of the secretary and employees shall be such as may be prescribed.

(12) The head office of the National Financial Reporting Authority shall be at New Delhi and the National Financial Reporting Authority may, meet at such other places in India as it deems fit.

(13) The National Financial Reporting Authority shall cause to be maintained such books of account and other books in relation to its accounts in such form and in such manner as the Central Government may, in consultation with the Comptroller and Auditor-General of India prescribe.

(14) The accounts of the National Financial Reporting Authority shall be audited by the Comptroller and Auditor-General of India at such intervals as may be specified by him and such accounts as certified by the Comptroller and Auditor-General of India together with the audit report thereon shall be forwarded annually to the Central Government by the National Financial Reporting Authority.

(15) The National Financial Reporting Authority shall prepare in such form and at such time for each financial year as may be

prescribed its annual report giving a full account of its activities during the financial year and forward a copy thereof to the Central Government and the Central Government shall cause the annual report and the audit report given by the Comptroller and Auditor-General of India to be laid before each House of Parliament.

Central Government to prescribe Accounting Standards (Sec.133):

The Central Government may prescribe the standards of accounting or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, constituted under Section 3 of the Chartered Accountants Act, 1949 (38 of 1949), in consultation with and after examination of the recommendations made by the National Financial Reporting Authority.

Financial Statement, Board's report, etc. (Sec.134):

[(1) The financial statement, including consolidated financial statement, if any, shall be approved by the Board of Directors before they are signed on behalf of the Board by the chairperson of the company where he is authorised by the Board or by two directors out of which one shall be managing director, if any, and the Chief Executive Officer, the Chief Financial Officer and the company secretary of the company, wherever they are appointed, or in the case of One Person Company, only by one director, for submission to the auditor for his report thereon.]

(2) The auditors' report shall be attached to every financial statement.

(3) There shall be attached to statements laid before a company in general meeting, a report by its Board of Directors, which shall include:

[(a) The web address, if any, where annual return referred to in sub-section (3) of section 92 has been placed];

(b) number of meetings of the Board;

(c) Directors' Responsibility Statement;

(ca) details in respect of frauds reported by auditors under sub-section (12) of Section 143 other than those which are reportable to the Central Government;

(d) a statement on declaration given by independent directors under sub-section (6) of Section 149;

(e) in case of a company covered under sub-section (1) of Section 178, company's policy on directors' appointment and remuneration including criteria for determining qualifications, positive attributes, independence of a director and other matters provided under sub-section (*3*) of Section 178;

(f) explanations or comments by the Board on every qualification, reservation or adverse remark or disclaimer made:

(i) by the auditor in his report; and

(ii) by the company secretary in practice in his secretarial audit report;

(g) particulars of loans, guarantees or investments under section 186;

(h) particulars of contracts or arrangements with related parties referred to in sub-section (1) of section 188 in the prescribed form;

(i) the state of the company's affairs;

(j) the amounts, if any, which it proposes to carry to any reserves;

(k) the amount, if any, which it recommends should be paid by way of dividend;

(l) material changes and commitments, if any, affecting the financial position of the company which have occurred between the end of the financial year of the company to which the financial statements relate and the date of the report;

(m) the conservation of energy, technology absorption, foreign exchange earnings and outgo, in such manner as may be prescribed;

(n) a statement indicating development and implementation of a risk management policy for the company including identification therein of elements of risk, if any, which in the opinion of the Board may threaten the existence of the company;

(o) the details about the policy developed and implemented by the company on corporate social responsibility initiatives taken during the year;

(p) in case of a listed company and every other public company having such paid-up share capital as may be prescribed, a statement indicating the manner in which formal [annual evaluation of the performance of the Board, its Committees and of individual directors has been made];

(q) such other matters as may be prescribed.

[Provided that where disclosures referred to in this sub-section have been included in the financial statements, such disclosures shall be referred to instead of being repeated in the Board's report:

Provided further that where the policy referred to in clause (e) or clause (o) is made available on company's website, if any, it shall be sufficient compliance of the requirements under such clauses if the salient features of the policy and any change therein are specified in brief in the Board's report and the web-address is indicated therein at which the complete policy is available.

(3A) The Central Government may prescribe an abridged Board's report, for the purpose of compliance with this section by One Person Company or small company.]

(4) The report of the Board of Directors to be attached to the financial statement under this section shall, in case of a One Person Company, mean a report containing explanations or comments by the Board on every qualification, reservation or adverse remark or disclaimer made by the auditor in his report.

(5) The Directors' Responsibility Statement referred to in clause (c) of sub-section (3) shall state that:

(a) in the preparation of the annual accounts, the applicable accounting standards had been followed along with proper explanation relating to material departures;

(b) the directors had selected such accounting policies and applied them consistently and made judgments and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company at the end of the financial year and of the profit and loss of the company for that period;

(c) the directors had taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of this Act for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities;

(d) the directors had prepared the annual accounts on a going concern basis; and

(e) the directors, in the case of a listed company, had laid down internal financial controls to be followed by the company and that such internal financial controls are adequate and were operating effectively.

Explanation: For the purposes of this clause, the term "internal financial controls" means the policies and procedures adopted by the company for ensuring the orderly and efficient conduct of its business, including adherence to company's policies, the safeguarding of its assets, the prevention and detection of frauds and errors, the accuracy and completeness of the accounting records, and the timely preparation of reliable financial information;

(f) the directors had devised proper systems to ensure compliance with the provisions of all applicable laws and that such systems were adequate and operating effectively.

(6) The Board's report and any annexures thereto under sub-section (3) shall be signed by its chairperson of the company if he is

authorised by the Board and where he is not so authorised, shall be signed by at least two directors, one of whom shall be a managing director, or by the director where there is one director.

(7) A signed copy of every financial statement, including consolidated financial statement, if any, shall be issued, circulated or published along with a copy each of:

(a) any notes annexed to or forming part of such financial statement;

(b) the auditor's report; and

(c) the Board's report referred to in sub-section (3).

(8) If a company contravenes the provisions of this section, the company shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.

Corporate Social Responsibility (Sec.135)

(1) Every company having net worth of rupees five hundred crore or more, or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during [the immediately preceding financial year] shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which at least one director shall be an independent director.

[Provided that where a company is not required to appoint an independent director under sub-section (4) of section 149, it shall have in its Corporate Social Responsibility Committee two or more directors.]

(2) The Board's report under sub-section (3) of section 134 shall disclose the composition of the Corporate Social Responsibility Committee.

(3) The Corporate Social Responsibility Committee shall:

(a) formulate and recommend to the Board, a Corporate Social Responsibility Policy which shall indicate the activities to be undertaken by the company [in areas or subject, specified in Schedule VII];

(b) recommend the amount of expenditure to be incurred on the activities referred to in clause (a); and

(c) monitor the Corporate Social Responsibility Policy of the company from time to time.

(4) The Board of every company referred to in sub-section (1) shall:

(a) after taking into account the recommendations made by the Corporate Social Responsibility Committee, approve the Corporate Social Responsibility Policy for the company and disclose contents of such Policy in its report and also place it on the company's website, if any, in such manner as may be prescribed; and

(b) ensure that the activities as are included in Corporate Social Responsibility Policy of the company are undertaken by the company.

(5) The Board of every company referred to in sub-section (1), shall ensure that the company spends, in every financial year, at least two per cent. of the average net profits of the company made during the three immediately preceding financial years, or where the company has not completed the period of three financial years since its incorporation, during such immediately preceding financial years in pursuance of its Corporate Social Responsibility Policy:

Provided that the company shall give preference to the local area and areas around it where it operates, for spending the amount earmarked for Corporate Social Responsibility activities:

Provided further that if the company fails to spend such amount, the Board shall, in its report made under clause (o) of sub-section

(3) of section 134, specify the reasons for not spending the amount and, unless the unspent amount relates to any ongoing project referred to in sub-section (6), transfer such unspent amount to a Fund specified in Schedule VII, within a period of six months of the expiry of the financial year.

[Explanation: For the purposes of this section "net profit" shall not include such sums as may be prescribed, and shall be calculated in accordance with the provisions of section 198].

(6) Any amount remaining unspent under sub-section (5), pursuant to any ongoing project, fulfilling such conditions as may be prescribed, undertaken by a company in persuance of its Corporate Social Responsibility Policy, shall be transferred by the company within a period of thirty days from the end of the financial year to a special account to be opened by the company in that behalf for that financial year in any scheduled bank to be called the Unspent Corporate Social Responsibility Account, and such amount shall be spent by the company in pursuance of its obligation towards the Corporate Social Responsibility Policy within a period of three financial years from the date of such transfer, failing which, the company shall transfer the same to a Fund specified in Schedule VII, within a period of thirty days from the date of completion of the third financial year.

(7) If a company contravenes the provisions of sub-section (5) or sub-section (6), the company shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to twenty-five lakh rupees and every officer of such company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.

(8) The Central Government may give such general or special directions to a company or class of companies as it considers necessary to ensure compliance of provisions of this section and

such company or class of companies shall comply with such directions.

Activities which may be included by Companies in their Corporate Social Responsibility Policies

Activities relating to –

i Eradicating extreme hunger and poverty.

ii Promotion of education.

iii Promotion gender quality and empowering women.

iv Reducing child morality and improving maternal health.

v Combating human immune-deficiency virus, acquired immune deficiency syndrome, malaria and other diseases.

vi Ensuring environmental sustainability.

vii Employment enhancing vocational skills.

viii Social business projects.

ix Contribution to the Prime Minister's National Relief Fund or any other fund set up by the Central Government or the State Governments for socio-economic development and relief and funds for the welfare of the Schedule Castes, the Schedule Tribes, other backward classes, minorities and women, and

x Such other matters as may be prescribed.

Right of member to copies of audited financial statement (Sec.136)

(1) [xxx], a copy of the financial statements, including consolidated financial statements, if any, auditor's report and every other document required by law to be annexed or attached to the financial statements, which are to be laid before a company in its general meeting, shall be sent to every member of the company, to every trustee for the debenture-holder of any debentures issued by the company, and to all persons other than such member or trustee,

being the person so entitled, not less than twenty-one days before the date of the meeting:

Provided that if the copies of the documents are sent less than twenty-one days before the date of the meeting, they shall, notwithstanding that fact, be deemed to have been duly sent if it is so agreed by members—

(a) holding, if the company has a share capital, majority in number entitled to vote and who represent not less than ninety-five per cent. of such part of the paid-up share capital of the company as gives a right to vote at the meeting; or

(b) having, if the company has no share capital, not less than ninetyfive per cent. of the total voting power exercisable at the meeting:

Provided further that in the case of a listed company, the provisions of this sub-section shall be deemed to be complied with, if the copies of the documents are made available for inspection at its registered office during working hours for a period of twenty-one days before the date of the meeting and a statement containing the salient features of such documents in the prescribed form or copies of the documents, as the company may deem fit, is sent to every member of the company and to every trustee for the holders of any debentures issued by the company not less than twenty-one days before the date of the meeting unless the shareholders ask for full financial statements:

Provided also that the Central Government may prescribe the manner of circulation of financial statements of companies having such net worth and turnover as may be prescribed:

Provided also that a listed company shall also place its financial statements including consolidated financial statements, if any, and all other documents required to be attached thereto, on its website, which is maintained by or on behalf of the company:

[Provided also that every listed company having a subsidiary or subsidiaries shall place separate audited accounts in respect of each of subsidiary on its website, if any:

Provided also that a listed company which has a subsidiary incorporated outside India (herein referred to as "foreign subsidiary"):

(a) where such foreign subsidiary is statutorily required to prepare consolidated financial statement under any law of the country of its incorporation, the requirement of this proviso shall be met if consolidated financial statement of such foreign subsidiary is placed on the website of the listed company;

(b) where such foreign subsidiary is not required to get its financial statement audited under any law of the country of its incorporation and which does not get such financial statement audited, the holding Indian listed company may place such unaudited financial statement on its website and where such financial statement is in a language other than English, a translated copy of the financial statement in English shall also be placed on the website].

(2) A company shall allow every member or trustee of the holder of any debentures issued by the company to inspect the documents stated under sub-section (1) at its registered office during business hours.

[Provided that every company having a subsidiary or subsidiaries shall provide a copy of separate audited or unaudited financial statements, as the case may be, as prepared in respect of each of its subsidiary to any member of the company who asks for it.]

(3) If any default is made in complying with the provisions of this section, the company shall be liable to a penalty of twenty-five thousand rupees and every officer of the company who is in default shall be liable to a penalty of five thousand rupees.

Copy of financial statement to be filed with Registrar (Sec.137)

(1) A copy of the financial statements, including consolidated financial statement, if any, along with all the documents which are required to be or attached to such financial statements under this Act, duly adopted at the annual general meeting of the company, shall be filed with the Registrar within thirty days of the date of annual general meeting in such manner, with such fees or additional fees as may be prescribed [xxx]:

Provided that where the financial statements under sub-section (*1*) are not adopted at annual general meeting or adjourned annual general meeting, such unadopted financial statements along with the required documents under sub-section (1) shall be filed with the Registrar within thirty days of the date of annual general meeting and the Registrar shall take them in his records as provisional till the financial statements are filed with him after their adoption in the adjourned annual general meeting for that purpose:

Provided further that financial statements adopted in the adjourned annual general meeting shall be filed with the Registrar within thirty days of the date of such adjourned annual general meeting with such fees or such additional fees as may be prescribed [xxx]:

Provided also that a One Person Company shall file a copy of the financial statements duly adopted by its member, along with all the documents which are required to be attached to such financial statements, within one hundred eighty days from the closure of the financial year:

Provided also that a company shall, along with its financial statements to be filed with the Registrar, attach the accounts of its subsidiary or subsidiaries which have been incorporated outside India and which have not established their place of business in India.

[Provided also that in the case of a subsidiary which has been incorporated outside India (herein referred to as "foreign subsidiary"), which is not required to get its financial statement audited under any

law of the country of its incorporation and which does not get such financial statement audited, the requirements of the fourth proviso shall be met if the holding Indian company files such unaudited financial statement along with a declaration to this effect and where such financial statement is in a language other than English, along with a translated copy of the financial statement in English].

(2) Where the annual general meeting of a company for any year has not been held, the financial statements along with the documents required to be attached under sub-section (1), duly signed along with the statement of facts and reasons for not holding the annual general meeting shall be filed with the Registrar within thirty days of the last date before which the annual general meeting should have been held and in such manner, with such fees or additional fees as may be prescribed [xxx].

(3) If a company fails to file the copy of the financial statements under sub-section (1) or sub-section (2), as the case may be, before the expiry of the period specified therein, the company shall be liable to a penalty of one thousand rupees for every day during which the failure continues but which shall not be more than ten lakh rupees, and the managing director and the Chief Financial Officer of the company, if any, and, in the absence of the managing director and the Chief Financial Officer, any other director who is charged by the Board with the responsibility of complying with the provisions of this section, and, in the absence of any such director, all the directors of the company, shall be liable to a penalty of one lakh rupees and in case of continuing failure, with a further penalty of one hundred rupees for each day after the first during which such failure continues, subject to a maximum of five lakh rupees.

Internal Audit (Sec.138)

(1) Such class or classes of companies as may be prescribed shall be required to appoint an internal auditor, who shall either be a chartered accountant or a cost accountant, or such other professional as may be decided by the Board to conduct internal audit of the functions and activities of the company.

(2) The Central Government may, by rules, prescribe the manner and the intervals in which the internal audit shall be conducted and reported to the Board.

Lecture – XIV
AUDIT AND AUDITORS

Chapter X containing Sections 139 to 148 of the Companies Act, 2013 lays down the provisions related to Audit and Auditors as stated below –

Appointment of auditors (Sec.139)

(1) Subject to the provisions of this Chapter, every company shall, at the first annual general meeting, appoint an individual or a firm as an auditor who shall hold office from the conclusion of that meeting till the conclusion of its sixth annual general meeting and thereafter till the conclusion of every sixth meeting and the manner and procedure of selection of auditors by the members of the company at such meeting shall be such as may be prescribed:

[xxx]

Provided further that before such appointment is made, the written consent of the auditor to such appointment, and a certificate from him or it that the appointment, if made, shall be in accordance with the conditions as may be prescribed, shall be obtained from the auditor:

Provided also that the certificate shall also indicate whether the auditor satisfies the criteria provided in section 141:

Provided also that the company shall inform the auditor concerned of his or its appointment, and also file a notice of such appointment with the Registrar within fifteen days of the meeting in which the auditor is appointed.

Explanation: For the purposes of this Chapter, "appointment" includes re-appointment.

(2) No listed company or a company belonging to such class or classes of companies as may be prescribed, shall appoint or re-appoint:

(a) an individual as auditor for more than one term of five consecutive years; and

(b) an audit firm as auditor for more than two terms of five consecutive years:

Provided that:

(i) an individual auditor who has completed his term under clause (a) shall not be eligible for re-appointment as auditor in the same company for five years from the completion of his term;

(ii) an audit firm which has completed its term under clause (b), shall not be eligible for re-appointment as auditor in the same company for five years from the completion of such term:

Provided further that as on the date of appointment no audit firm having a common partner or partners to the other audit firm, whose tenure has expired in a company immediately preceding the financial year, shall be appointed as auditor of the same company for a period of five years:

Provided also that every company, existing on or before the commencement of this Act which is required to comply with provisions of this sub-section, shall comply with the requirements of this sub-section within three years from the date of commencement of this Act:

Provided also that, nothing contained in this sub-section shall prejudice the right of the company to remove an auditor or the right of the auditor to resign from such office of the company.

(3) Subject to the provisions of this Act, members of a company may resolve to provide that:

(a) in the audit firm appointed by it, the auditing partner and his team shall be rotated at such intervals as may be resolved by members; or

(b) the audit shall be conducted by more than one auditor.

(4) The Central Government may, by rules, prescribe the manner in which the companies shall rotate their auditors in pursuance of sub-section (2).

Explanation: For the purposes of this Chapter, the word "firm" shall include a limited liability partnership incorporated under the Limited Liability Partnership Act, 2008 (6 of 2009).

(5) Notwithstanding anything contained in sub-section (1), in the case of a Government company or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, the Comptroller and Auditor-General of India shall, in respect of a financial year, appoint an auditor duly qualified to be appointed as an auditor of companies under this Act, within a period of one hundred and eighty days from the commencement of the financial year, who shall hold office till the conclusion of the annual general meeting.

(6) Notwithstanding anything contained in sub-section (1), the first auditor of a company, other than a Government company, shall be appointed by the Board of Directors within thirty days from the date of registration of the company and in the case of failure of the Board to appoint such auditor, it shall inform the members of the company, who shall within ninety days at an extraordinary general meeting appoint such auditor and such auditor shall hold office till the conclusion of the first annual general meeting.

(7) Notwithstanding anything contained in sub-section (1) or sub-section (5), in the case of a Government company or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government, or Governments, or partly by the Central Government and partly by one or more State Governments, the first auditor shall be appointed by the Comptroller and Auditor-General of India within sixty days from the date of registration of the company and in case the Comptroller and Auditor-General of India does not appoint such auditor within the said period, the Board of Directors of the company shall appoint such auditor within the next thirty days; and in the case of failure of the Board to

appoint such auditor within the next thirty days, it shall inform the members of the company who shall appoint such auditor within the sixty days at an extraordinary general meeting, who shall hold office till the conclusion of the first annual general meeting.

(8) Any casual vacancy in the office of an auditor shall;

(i) in the case of a company other than a company whose accounts are subject to audit by an auditor appointed by the Comptroller and Auditor-General of India, be filled by the Board of Directors within thirty days, but if such casual vacancy is as a result of the resignation of an auditor, such appointment shall also be approved by the company at a general meeting convened within three months of the recommendation of the Board and he shall hold the office till the conclusion of the next annual general meeting;

(ii) in the case of a company whose accounts are subject to audit by an auditor appointed by the Comptroller and Auditor-General of India, be filled by the Comptroller and Auditor-General of India within thirty days;

Provided that in case the Comptroller and Auditor-General of India does not fill the vacancy within the said period, the Board of Directors shall fill the vacancy within next thirty days.

(9) Subject to the provisions of sub-section (1) and the rules made thereunder, a retiring auditor may be re-appointed at an annual general meeting, if:

(a) he is not disqualified for re-appointment;

(b) he has not given the company a notice in writing of his unwillingness to be re-appointed; and

(c) a special resolution has not been passed at that meeting appointing some other auditor or providing expressly that he shall not be re-appointed.

(10) Where at any annual general meeting, no auditor is appointed or re-appointed, the existing auditor shall continue to be the auditor of the company.

(11) Where a company is required to constitute an Audit Committee under section 177, all appointments, including the filling of a casual vacancy of an auditor under this section shall be made after taking into account the recommendations of such committee.

Removal, resignation of auditor and giving of special Notice (Sec.140)

(1) The auditor appointed under section 139 may be removed from his office before the expiry of his term only by a special resolution of the company, after obtaining the previous approval of the Central Government in that behalf in the prescribed manner:

Provided that before taking any action under this sub-section, the auditor concerned shall be given a reasonable opportunity of being heard.

(2) The auditor who has resigned from the company shall file within a period of thirty days from the date of resignation, a statement in the prescribed form with the company and the Registrar, and in case of companies referred to in sub-section (5) of section 139, the auditor shall also file such statement with the Comptroller and Auditor-General of India, indicating the reasons and other facts as may be relevant with regard to his resignation.

(3) If the auditor does not comply with the provisions of sub-section (2), he or it shall be liable to a penalty of fifty thousand rupees or an amount equal to the remuneration of the auditor, whichever is less, and in case of continuing failure, with a further penalty of five hundred rupees for each day after the first during which such failure continues, subject to a maximum of five lakh rupees

(4) (i) Special notice shall be required for a resolution at an annual general meeting appointing as auditor a person other than a retiring auditor, or providing expressly that a retiring auditor shall not be re-appointed, except where the retiring auditor has completed a consecutive tenure of five years or, as the case may be, ten years, as provided under sub-section (2) of section 139.

(ii) On receipt of notice of such a resolution, the company shall forthwith send a copy thereof to the retiring auditor.

(iii) Where notice is given of such a resolution and the retiring auditor makes with respect thereto representation in writing to the

company (not exceeding a reasonable length) and requests its notification to members of the company, the company shall, unless the representation is received by it too late for it to do so:

(a) in any notice of the resolution given to members of the company, state the fact of the representation having been made; and

(b) send a copy of the representation to every member of the company to whom notice of the meeting is sent, whether before or after the receipt of the representation by the company,

and if a copy of the representation is not sent as aforesaid because it was received too late or because of the company's default, the auditor may (without prejudice to his right to be heard orally) require that the representation shall be read out at the meeting:

Provided that if a copy of representation is not sent as aforesaid, a copy thereof shall be filed with the Registrar:

Provided further that if the Tribunal is satisfied on an application either of the company or of any other aggrieved person that the rights conferred by this sub-section are being abused by the auditor, then, the copy of the representation may not be sent and the representation need not be read out at the meeting.

(5) Without prejudice to any action under the provisions of this Act or any other law for the time being in force, the Tribunal either *suo motu* or on an application made to it by the Central Government or by any person concerned, if it is satisfied that the auditor of a company has, whether directly or indirectly, acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its directors or officers, it may, by order, direct the company to change its auditors:

Provided that if the application is made by the Central Government and the Tribunal is satisfied that any change of the auditor is required, it shall within fifteen days of receipt of such application, make an order that he shall not function as an auditor and the Central Government may appoint another auditor in his place:

Provided further that an auditor, whether individual or firm, against whom final order has been passed by the Tribunal under this

section shall not be eligible to be appointed as an auditor of any company for a period of five years from the date of passing of the order and the auditor shall also be liable for action under section 447.

Explanation I: It is hereby clarified that the case of a firm, the liability shall be of the firm and that of every partner or partners who acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to, the company or its director or officers.

Explanation II: For the purposes of this Chapter the word "auditor" includes a firm of auditors.

Eligibility, qualifications and disqualifications of auditors (Sec.141)

(1) A person shall be eligible for appointment as an auditor of a company only if he is a chartered accountant:

Provided that a firm whereof majority of partners practising in India are qualified for appointment as aforesaid may be appointed by its firm name to be auditor of a company.

(2) Where a firm including a limited liability partnership is appointed as an auditor of a company, only the partners who are chartered accountants shall be authorised to act and sign on behalf of the firm.

(3) The following persons shall not be eligible for appointment as an auditor of a company, namely:

(a) a body corporate other than a limited liability partnership registered under the Limited Liability Partnership Act, 2008 (6 of 2009);

(b) an officer or employee of the company;

(c) a person who is a partner, or who is in the employment, of an officer or employee of the company;

(d) a person who, or his relative or partner:

(i) is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company:

Provided that the relative may hold security or interest in the company of face value not exceeding one thousand rupees or such sum as may be prescribed;

(ii) is indebted to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of such amount as may be prescribed; or

(iii) has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, for such amount as may be prescribed;

(e) a person or a firm who, whether directly or indirectly, has business relationship with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company of such nature as may be prescribed;

(f) a person whose relative is a director or is in the employment of the company as a director or key managerial personnel;

(g) a person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such persons or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies;

(h) a person who has been convicted by a court of an offence involving fraud and a period of ten years has not elapsed from the date of such conviction;

[(i) (i) a person who, directly or indirectly, renders any service referred to in section 144 to the company or its holding company or its subsidiary company.

Explanation. For the purposes of this clause, the term "directly or indirectly" shall have the meaning assigned to it in the Explanation to section 144].

(4) Where a person appointed as an auditor of a company incurs any of the disqualifications mentioned in sub-section (3) after his appointment, he shall vacate his office as such auditor and such

vacation shall be deemed to be a casual vacancy in the office of the auditor.

Remuneration of Auditors (Sec.142)

(1) The remuneration of the auditor of a company shall be fixed in its general meeting or in such manner as may be determined therein:

Provided that the Board may fix remuneration of the first auditor appointed by it.

(2) The remuneration under sub-section (1) shall, in addition to the fee payable to an auditor, include the expenses, if any, incurred by the auditor in connection with the audit of the company and any facility extended to him but does not include any remuneration paid to him for any other service rendered by him at the request of the company.

Powers and Duties of Auditors and Auditing Standards (Sec.143)

(1) Every auditor of a company shall have a right of access at all times to the books of account and vouchers of the company, whether kept at the registered office of the company or at any other place and shall be entitled to require from the officers of the company such information and explanation as he may consider necessary for the performance of his duties as auditor and amongst other matters inquire into the following matters, namely:

(a) whether loans and advances made by the company on the basis of security have been properly secured and whether the terms on which they have been made are prejudicial to the interests of the company or its members;

(b) whether transactions of the company which are represented merely by book entries are prejudicial to the interests of the company;

(c) where the company not being an investment company or a banking company, whether so much of the assets of the company as consist of shares, debentures and other securities

have been sold at a price less than that at which they were purchased by the company;

(d) whether loans and advances made by the company have been shown as deposits;

(e) whether personal expenses have been charged to revenue account;

(f) where it is stated in the books and documents of the company that any shares have been allotted for cash, whether cash has actually been received in respect of such allotment, and if no cash has actually been so received, whether the position as stated in the account books and the balance sheet is correct, regular and not misleading:

Provided that the auditor of a company which is a holding company shall also have the right of access to the records of all [its subsidiaries and associate companies] in so far as it relates to the consolidation of its financial statements with that of [its subsidiaries and associate companies].

(2) The auditor shall make a report to the members of the company on the accounts examined by him and on every financial statements which are required by or under this Act to be laid before the company in general meeting and the report shall after taking into account the provisions of this Act, the accounting and auditing standards and matters which are required to be included in the audit report under the provisions of this Act or any rules made thereunder or under any order made under sub-section (*11*) and to the best of his information and knowledge, the said accounts, financial statements give a true and fair view of the state of the company's affairs as at the end of its financial year and profit or loss and cash flow for the year and such other matters as may be prescribed.

(*3*) The auditor's report shall also state:

(a) whether he has sought and obtained all the information and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;

(b) whether, in his opinion, proper books of account as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purposes of his audit have been received from branches not visited by him;

(c) whether the report on the accounts of any branch office of the company audited under sub-section (8) by a person other than the company's auditor has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report;

(d) whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns;

(e) whether, in his opinion, the financial statements comply with the accounting standards;

(f) the observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company;

(g) whether any director is disqualified from being appointed as a director under sub-section (2) of section 164;

(h) any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;

(i) whether the company has adequate [internal financial controls with reference to financial statements] in place and the operating effectiveness of such controls;

(j) such other matters as may be prescribed.

(4) Where any of the matters required to be included in the audit report under this section is answered in the negative or with a qualification, the report shall state the reasons therefor.

(5) In the case of a Government company or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, the Comptroller and Auditor-General of India shall

appoint the auditor under sub-section (5) or sub-section (7) of Section 139 and direct such auditor the manner in which the accounts of the company are required to be audited and] thereupon the auditor so appointed shall submit a copy of the audit report to the Comptroller and Auditor-General of India which, among other things, include the directions, if any, issued by the Comptroller and Auditor-General of India, the action taken thereon and its impact on the accounts and financial statement of the company.

(6) The Comptroller and Auditor-General of India shall within sixty days from the date of receipt of the audit report under sub-section (5) have a right to:

(a) conduct a supplementary audit of the financial statement of the company by such person or persons as he may authorise in this behalf; and for the purposes of such audit, require information or additional information to be furnished to any person or persons, so authorised, on such matters, by such person or persons, and in such form, as the Comptroller and Auditor-General of India may direct; and

(b) comment upon or supplement such audit report:

Provided that any comments given by the Comptroller and Auditor-General of India upon, or supplement to, the audit report shall be sent by the company to every person entitled to copies of audited financial statements under sub-section (1) of section 136 and also be placed before the annual general meeting of the company at the same time and in the same manner as the audit report.

(7) Without prejudice to the provisions of this Chapter, the Comptroller and Auditor-General of India may, in case of any company covered under sub-section (5) or sub-section (7) of section 139, if he considers necessary, by an order, cause test audit to be conducted of the accounts of such company and the provisions of section 19A of the Comptroller and Auditor-General's (Duties, Powers and Conditions of Service) Act, 1971 (56 of 1971), shall apply to the report of such test audit.

(8) Where a company has a branch office, the accounts of that office shall be audited either by the auditor appointed for the company

(herein referred to as the company's auditor) under this Act or by any other person qualified for appointment as an auditor of the company under this Act and appointed as such under section 139, or where the branch office is situated in a country outside India, the accounts of the branch office shall be audited either by the company's auditor or by an accountant or by any other person duly qualified to act as an auditor of the accounts of the branch office in accordance with the laws of that country and the duties and powers of the company's auditor with reference to the audit of the branch and the branch auditor, if any, shall be such as may be prescribed:

Provided that the branch auditor shall prepare a report on the accounts of the branch examined by him and send it to the auditor of the company who shall deal with it in his report in such manner as he considers necessary.

(9) Every auditor shall comply with the auditing standards.

(10) The Central Government may prescribe the standards of auditing or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, constituted under section 3 of the Chartered Accountants Act, 1949 (38 of 1949.), in consultation with and after examination of the recommendations made by the National Financial Reporting Authority:

Provided that until any auditing standards are notified, any standard or standards of auditing specified by the Institute of Chartered Accountants of India shall be deemed to be the auditing standards.

(11) The Central Government may, in consultation with the National Financial Reporting Authority, by general or special order, direct, in respect of such class or description of companies, as may be specified in the order, that the auditor's report shall also include a statement on such matters as may be specified therein.

(12) Notwithstanding anything contained in this section, if an auditor of a company, in the course of the performance of his duties as auditor, has reason to believe that an offence of fraud involving such amount or amount as may be prescribed, is being or has been

committed in the company by its officers or employees, the auditor shall report the matter to the Central Government within such time and in such manner as may be prescribed:

Provided that in case of a fraud involving lesser than the specified amount, the auditor shall report the matter to the audit committee constituted under Section 177 or to the Board in other cases within such time and in such manner as may be prescribed:

Provided further that the companies, whose auditors have reported frauds under this sub-section to the audit committee or the Board but not reported to the Central Government, shall disclose the details about such frauds in the Board's report in such manner as may be prescribed.

(13) No duty to which an auditor of a company may be subject to shall be regarded as having been contravened by reason of his reporting the matter referred to in sub-section (12) if it is done in good faith.

(14) The provisions of this section shall *mutatis mutandis* apply to:

(a) the [cost accountant] conducting cost audit under section 148; or

(b) the company secretary in practice conducting secretarial audit under section 204.

(15) If any auditor, cost accountant or company secretary in practice do not comply with the provisions of sub-section (12), he shall be punishable with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees.

Auditor not to render certain services (Sec.144)

An auditor appointed under this Act shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, as the case may be, but which shall not include any of the following services (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company, namely:

(a) accounting and book keeping services;

(b) internal audit;

(c) design and implementation of any financial information system;

(d) actuarial services;

(e) investment advisory services;

(f) investment banking services;

(g) rendering of outsourced financial services;

(h) management services; and

(i) any other kind of services as may be prescribed:

Provided that an auditor or audit firm who or which has been performing any non-audit services on or before the commencement of this Act shall comply with the provisions of this section before the closure of the first financial year after the date of such commencement.

Explanation: For the purposes of this sub-section, the term "directly or indirectly" shall include rendering of services by the auditor:

(i) in case of auditor being an individual, either himself or through his relative or any other person connected or associated with such individual or through any other entity, whatsoever, in which such individual has significant influence or control, or whose name or trade mark or brand is used by such individual;

(ii) in case of auditor being a firm, either itself or through any of its partners or through its parent, subsidiary or associate entity or through any other entity, whatsoever, in which the firm or any partner of the firm has significant influence or control, or whose name or trade mark or brand is used by the firm or any of its partners.

Auditor to sign audit reports, etc. (Sec.145)

The person appointed as an auditor of the company shall sign the auditor's report or sign or certify any other document of the company in accordance with the provisions of sub-section (2) of section 141, and the qualifications, observations or comments on

financial transactions or matters, which have any adverse effect on the functioning of the company mentioned in the auditor's report shall be read before the company in general meeting and shall be open to inspection by any member of the company.

Auditors to attend general meeting (Sec.146)

All notices of, and other communications relating to, any general meeting shall be forwarded to the auditor of the company, and the auditor shall, unless otherwise exempted by the company, attend either by himself or through his authorised representative, who shall also be qualified to be an auditor, any general meeting and shall have right to be heard at such meeting on any part of the business which concerns him as the auditor.

Punishment for contravention (Sec.147)

(1) If any of the provisions of sections 139 to 146 (both inclusive) is contravened, the company shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than ten thousand rupees but which may extend to one lakh rupees, or with both.

(2) If an auditor of a company contravenes any of the provisions of section 139, section 143, section 144 or section 145, the auditor shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to [or four times the remuneration of the auditor, whichever is less]:

Provided that if an auditor has contravened such provisions knowingly or wilfully with the intention to deceive the company or its shareholders or creditors or tax authorities, he shall be punishable with imprisonment for a term which may extend to one year [and with fine which shall not be less than fifty thousand rupees but which may extend to twenty-five lakh rupees or eight times the remuneration of the auditor, whichever is less].

(3) Where an auditor has been convicted under sub-section (2), he shall be liable to:

(i) refund the remuneration received by him to the company; and

(ii) pay for damages to the company, statutory bodies or authorities [or to members or creditors of the company] for loss arising out of incorrect or misleading statements of particulars made in his audit report.

(4) The Central Government shall, by notification, specify any statutory body or authority or an officer for ensuring prompt payment of damages to the company or the persons under clause (*ii*) of sub-section (3) and such body, authority or officer shall after payment of damages to such company or persons file a report with the Central Government in respect of making such damages in such manner as may be specified in the said notification.

(*5*) Where, in case of audit of a company being conducted by an audit firm, it is proved that the partner or partners of the audit firm has or have acted in a fraudulent manner or abetted or colluded in any fraud by, or in relation to or by, the company or its directors or officers, the liability, whether civil or criminal as provided in this Act or in any other law for the time being in force, for such act shall be of the partner or partners concerned of the audit firm and of the firm jointly and severally.

[Provided that in case of criminal liability of an audit firm, in respect of liability other than fine, the concerned partner or partners, who acted in a fraudulent manner or abetted or, as the case may be, colluded in any fraud shall only be liable.]

Central Government to specify audit of items of cost in respect of certain companies (Sec.148)

(1) Notwithstanding anything contained in this Chapter, the Central Government may, by order, in respect of such class of companies engaged in the production of such goods or providing such services as may be prescribed, direct that particulars relating to the utilisation of material or labour or to other items of cost as may be prescribed shall also be included in the books of account kept by that class of companies:

Provided that the Central Government shall, before issuing such order in respect of any class of companies regulated under a special Act, consult the regulatory body constituted or established under such special Act.

(2) If the Central Government is of the opinion, that it is necessary to do so, it may, by order, direct that the audit of cost records of class of companies, which are covered under sub-section (1) and which have a net worth of such amount as may be prescribed or a turnover of such amount as may be prescribed, shall be conducted in the manner specified in the order.

(3) The audit under sub-section (2) shall be conducted by a [cost accountant] who shall be appointed by the Board on such remuneration as may be determined by the members in such manner as may be prescribed:

Provided that no person appointed under section 139 as an auditor of the company shall be appointed for conducting the audit of cost records:

Provided further that the auditor conducting the cost audit shall comply with the cost auditing standards.

Explanation: For the purposes of this sub-section, the expression "cost auditing standards" mean such standards as are issued by the [Institute of Cost Accountants of India], constituted under the Cost and Works Accountants Act, 1959 (23 of 1959), with the approval of the Central Government.

(4) An audit conducted under this section shall be in addition to the audit conducted under section 143.

(5) The qualifications, disqualifications, rights, duties and obligations applicable to auditors under this Chapter shall, so far as may be applicable, apply to a cost auditor appointed under this section and it shall be the duty of the company to give all assistance and facilities to the cost auditor appointed under this section for auditing the cost records of the company:

Provided that the report on the audit of cost records shall be submitted by the [cost accountant] to the Board of Directors of the company.

(6) A company shall within thirty days from the date of receipt of a copy of the cost audit report prepared in pursuance of a direction under sub-section (2) furnish the Central Government with such report along with full information and explanation on every reservation or qualification contained therein.

(7) If, after considering the cost audit report referred to under this section and the information and explanation furnished by the company under sub-section (6), the Central Government is of the opinion that any further information or explanation is necessary, it may call for such further information and explanation and the company shall furnish the same within such time as may be specified by that Government.

(8) If any default is made in complying with the provisions of this section:

(a) the company and every officer of the company who is in default shall be punishable in the manner as provided in sub-section (1) of section 147;

(b) the cost auditor of the company who is in default shall be punishable in the manner as provided in sub-sections (2) to (4) of section 147.

Lecture – XV

INSPECTION, INQUIRY AND INVESTIGATION

Chapter XIV containing Sections 206 to 229 of the Companies Act, 2013 lays down the provisions relating to 'Inspection, Inquiry and Investigation'.

Inspection: Section 206 of the Companies Act 2013 deals with inspection of documents and books and papers of any company. The section empowers the Registrar or Inspectors appointed by Central Government to conduct inspection in order to ascertain that all the transactions have been validly entered into and recorded in appropriate books and those applicable laws, rules and procedures have been compiled by the company.

Power to call for information, inspect books and conduct inquiries (Sec.206)

(1) Where on a scrutiny of any document filed by a company or on any information received by him, the Registrar is of the opinion that any further information or explanation or any further documents relating to the company is necessary, he may by a written notice require the company:

(*a*) to furnish in writing such information or explanation; or

(*b*) to produce such documents,

within such reasonable time, as may be specified in the notice.

1.Company's duty to furnish information:

(2) On the receipt of a notice under sub-section (*1*), it shall be the duty of the company and of its officers concerned to furnish such information or explanation to the best of their knowledge and power and to produce the documents to the Registrar within the time specified or extended by the Registrar:

Provided that where such information or explanation relates to any past period, the officers who had been in the employment of the company for such period, if so called upon by the Registrar through

a notice served on them in writing, shall also furnish such information or explanation to the best of their knowledge.

2.Second notice by Registrar:

If no information or explanation is furnished to the Registrar within the time specified under sub-section (*1*) or if the Registrar on an examination of the documents furnished is of the opinion that the information or explanation furnished is inadequate or if the Registrar is satisfied on a scrutiny of the documents furnished that an unsatisfactory state of affairs exists in the company and does not disclose a full and fair statement of the information required, he may, by another written notice, call on the company to produce for his inspection such further books of account, books, papers and explanations as he may require at such place and at such time as he may specify in the notice:

Provided that before any notice is served under this sub-section, the Registrar shall record his reasons in writing for issuing such notice.

(*4*) If the Registrar is satisfied on the basis of information available with or furnished to him or on a representation made to him by any person that the business of a company is being carried on for a fraudulent or unlawful purpose or not in compliance with the provisions of this Act or if the grievances of investors are not being addressed, the Registrar may, after informing the company of the allegations made against it by a written order, call on the company to furnish in writing any information or explanation on matters specified in the order within such time as he may specify therein and carry out such inquiry as he deems fit after providing the company a reasonable opportunity of being heard:

Provided that the Central Government may, if it is satisfied that the circumstances so warrant, direct the Registrar or an inspector appointed by it for the purpose to carry out the inquiry under this sub-section:

Provided further that where business of a company has been or is being carried on for a fraudulent or unlawful purpose, every

officer of the company who is in default shall be punishable for fraud in the manner as provided in section 447.

3. Inspection of Books and Papers:

(5) Without prejudice to the foregoing provisions of this section, the Central Government may, if it is satisfied that the circumstances so warrant, direct inspection of books and papers of a company by an inspector appointed by it for the purpose.

4. Penalty:

(7) If a company fails to furnish any information or explanation or produce any document required under this section, the company and every officer of the company, who is in default shall be punishable with a fine which may extend to one lakh rupees and in the case of a continuing failure, with an additional fine which may extend to five hundred rupees for every day after the first during which the failure continues.

Conduct of inspection and inquiry (Sec.207)

1. Company's duty to furnish information:

(1) Where a Registrar or inspector calls for the books of account and other books and papers under section 206, it shall be the duty of every director, officer or other employee of the company to produce all such documents to the Registrar or inspector and furnish him with such statements, information or explanations in such form as the Registrar or inspector may require and shall render all assistance to the Registrar or inspector in connection with such inspection.

2.Make marks on inspection:

(2) The Registrar or inspector, making an inspection or inquiry under section 206 may, during the course of such inspection or inquiry, as the case may be:

(*a*) make or cause to be made copies of books of account and other books and papers; or

(*b*) place or cause to be placed any marks of identification in such books in token of the inspection having been made.

3. Powers of Civil Court vested on Registrar:

(*3*) Notwithstanding anything contained in any other law for the time being in force or in any contract to the contrary, the Registrar or inspector making an inspection or inquiry shall have all the powers as are vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908), while trying a suit in respect of the following matters, namely:

(*a*) the discovery and production of books of account and other documents, at such place and time as may be specified by such Registrar or inspector making the inspection or inquiry;

(*b*) summoning and enforcing the attendance of persons and examining them on oath; and

(*c*) inspection of any books, registers and other documents of the company at any place.

4. Penalty:

(*4*) (*i*) If any director or officer of the company disobeys the direction issued by the Registrar or the inspector under this section, the director or the officer shall be punishable with imprisonment which may extend to one year and with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.

(*ii*) If a director or an officer of the company has been convicted of an offence under this section, the director or the officer shall, on and from the date on which he is so convicted, be deemed to have vacated his office as such and on such vacation of office, shall be disqualified from holding an office in any company.

Report on inspection made (Sec.208)

The Registrar or inspector shall, after the inspection of the books of account or an inquiry under section 206 and other books and papers of the company under section 207, submit a report in writing to the Central Government along with such documents, if any, and such report may, if necessary, include a recommendation that further investigation into the affairs of the company is necessary giving his reasons in support.

Search and Seizure (Sec.209)

(*1*) Where, upon information in his possession or otherwise, the Registrar or inspector has reasonable ground to believe that the books and papers of a company, or relating to the key managerial personnel or any director or auditor or company secretary in practice if the company has not appointed a company secretary, are likely to be destroyed, mutilated, altered, falsified or secreted, he may, after obtaining an order from the Special Court for the seizure of such books and papers:

(*a*) enter, with such assistance as may be required, and search, the place or places where such books or papers are kept; and

(*b*) seize such books and papers as he considers necessary after allowing the company to take copies of, or extracts from, such books or papers at its cost.

(*2*) The Registrar or inspector shall return the books and papers seized under sub-section (*1*), as soon as may be, and in any case not later than one hundred and eightieth day after such seizure, to the company from whose custody or power such books or papers were seized:

Provided that the books and papers may be called for by the Registrar or inspector for a further period of one hundred and eighty days by an order in writing if they are needed again:

Provided further that the Registrar or inspector may, before returning such books and papers as aforesaid, take copies of, or extracts from them or place identification marks on them or any part thereof or deal with the same in such other manner as he considers necessary.

(*3*) The provisions of the Code of Criminal Procedure, 1973 (2 of 1974) relating to searches or seizures shall apply, *mutatis mutandis,* to every search and seizure made under this section.

Investigation into affairs of company (Sec.210)

(*1*) Where the Central Government is of the opinion, that it is necessary to investigate into the affairs of a company:

(*a*) on the receipt of a report of the Registrar or inspector under section 208;

(*b*) on intimation of a special resolution passed by a company that the affairs of the company ought to be investigated; or

(*c*) in public interest,

it may order an investigation into the affairs of the company.

(*2*) Where an order is passed by a court or the Tribunal in any proceedings before it that the affairs of a company ought to be investigated, the Central Government shall order an investigation into the affairs of that company.

(*3*) For the purposes of this section, the Central Government may appoint one or more persons as inspectors to investigate into the affairs of the company and to report thereon in such manner as the Central Government may direct.

Investigation by the Tribunal in to Company's affairs in other cases (Sec.213)

The Tribunal may:

(*a*) on an application made by:

(*i*) not less than one hundred members or members holding not less than one-tenth of the total voting power, in the case of a company having a share capital; or

(*ii*) not less than one-fifth of the persons on the company's register of members, in the case of a company having no share capital,

and supported by such evidence as may be necessary for the purpose of showing that the applicants have good reasons for seeking an order for conducting an investigation into the affairs of the company; or

(*b*) on an application made to it by any other person or otherwise, if it is satisfied that there are circumstances suggesting that:

(*i*) the business of the company is being conducted with intent to defraud its creditors, members or any other person or

otherwise for a fraudulent or unlawful purpose, or in a manner oppressive to any of its members or that the company was formed for any fraudulent or unlawful purpose:

(*ii*) persons concerned in the formation of the company or the management of its affairs have in connection therewith been guilty of fraud, misfeasance or other misconduct towards the company or towards any of its members; or

(*iii*) the members of the company have not been given all the information with respect to its affairs which they might reasonably expect, including information relating to the calculation of the commission payable to a managing or other director, or the manager, of the company,

order, after giving a reasonable opportunity of being heard to the parties concerned, that the affairs of the company ought to be investigated by an inspector or inspectors appointed by the Central Government and where such an order is passed, the Central Government shall appoint one or more competent persons as inspectors to investigate into the affairs of the company in respect of such matters and to report thereupon to it in such manner as the Central Government may direct:

Provided that if after investigation it is proved that:

(*i*) the business of the company is being conducted with intent to defraud its creditors, members or any other persons or otherwise for a fraudulent or unlawful purpose, or that the company was formed for any fraudulent or unlawful purpose: or

(*ii*) any person concerned in the formation of the company or the management of its affairs have in connection therewith been guilty of fraud,

then, every officer of the company who is in default and the person or persons concerned in the formation of the company or the management of its affairs shall be punishable for fraud in the manner as provided in section 447.

Security for payment of costs and expenses of investigation (Sec.214)

Where an investigation is ordered by the Central Government in pursuance of clause (*b*) of sub-section (*1*) of section 210, or in pursuance of an order made by the Tribunal under section 213, the Central Government may before appointing an inspector under sub-section (*3*) of section 210 or clause (*b*) of section 213, require the applicant to give such security not exceeding twenty-five thousand rupees as may be prescribed, as it may think fit, for payment of the costs and expenses of the investigation and such security shall be refunded to the applicant if the investigation results in prosecution.

Firm, body corporate or association not to be appointed as inspector (Sec.215)

No firm, body corporate or other association shall be appointed as an inspector.

Investigation of ownership of company (Sec.216)

(*1*) Where it appears to the Central Government that there is a reason so to do, it may appoint one or more inspectors to investigate and report on matters relating to the company, and its membership for the purpose of determining the true persons:

(*a*) who are or have been financially interested in the success or failure, whether real or apparent, of the company; or

(*b*) who are or have been able to control or to materially influence the policy of the company [or;

(c) who have or had beneficial interest in shares of a company or who are or have been beneficial owners or significant beneficial owner of a company].

(*2*) Without prejudice to its powers under sub-section (*1*), the Central Government shall appoint one or more inspectors under that sub-section, if the Tribunal, in the course of any proceeding before it, directs by an order that the affairs of the company ought to be investigated as regards the membership of the company and other matters relating to the company, for the purposes specified in sub-section (*1*).

(*3*) While appointing an inspector under sub-section (*1*), the Central Government may define the scope of the investigation,

whether as respects the matters or the period to which it is to extend or otherwise, and in particular, may limit the investigation to matters connected with particular shares or debentures.

(*4*) Subject to the terms of appointment of an inspector, his powers shall extend to the investigation of any circumstances suggesting the existence of any arrangement or understanding which, though not legally binding, is or was observed or is likely to be observed in practice and which is relevant for the purposes of his investigation.

Procedure, powers, etc. of inspectors (Sec.217)

(1) It shall be the duty of all officers and other employees and agents including the former officers, employees and agents of a company which is under investigation in accordance with the provisions contained in this Chapter, and where the affairs of any other body corporate or a person are investigated under Section 219, of all officers and other employees and agents including former officers, employees and agents of such body corporate or a person-

a. To preserve and to produce to an inspector or any person authorized by him in this behalf all books and papers of, or relating to, the company or, as the case may be, relating to the other body corporate or the person, which are in their custody or power, and

b. Otherwise to give to the inspector all assistance in connection with the investigation which they are reasonably able to give.

(2) The inspector may require any body corporate, other than a body corporate referred to in sub-section (1), to furnish such information to, or produce such books and papers before him or any person authorized by him in this behalf as he may consider necessary, if the furnishing of such information or the production of such books and papers is relevant or necessary for the purposes of his investigation.

(3) The inspector shall not keep in his custody any books and papers produced under sub-section (1) or sub-section (2) for more than one hundred and eighty days and return the same to the company, body corporate, firm or individual by whom or on whose behalf the books and papers were produced:

Provided that the book and papers may be called for by the inspector if they are needed again for a further period of one hundred and eighty days by an order in writing.

(4) An inspector may examine on oath -

a. Any of the persons referred to in sub-section (1), and

b. With the prior approval of the Central Government, and other person,

In relation to the affairs of the company, or other body corporate or person, as the case may be, and for that purpose may require any of those persons to appear before him personally:

Provided that in case of an investigation under Section 212, the prior approval of Director, serious Fraud Investigation Office shall be sufficient under clause (b).

(5) Notwithstanding anything contained in any other law for the time being in force or in any contract to the contrary, the inspector, being an officer of the Central Government, making an investigation under this Chapter shall have all the powers as are vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908), while trying a suit in respect of the following matters, namely -

a. The discovery and production of books of account and other documents, at such place and time as may be specified by such person.

b. Summoning and enforcing the attendance of persons and examining them on oath; and

c. Inspection of any books, registers and other documents of the company at any place.

(6) (i) If any director or officer of the company disobeys the direction issued by the Registrar or the inspector under this section, the director or the officer shall be punishable with imprisonment which may extend to one year and with five which shall not be less than twenty five thousand rupees but which may extend to one lakh rupees.

(ii) If a director or an officer of the company has been convicted of an offence under this section, the director or the officer shall, on and from the date on which he is so convicted, be deemed to have vacated his office as such and on such vacation of office, shall be disqualified from holding an office in any company.

(7) The notes of any examination under sub-section (4) shall be taken down in writing and shall be read over to, or by, and signed by, the person examined, and may thereafter be used in evidence against him.

(8) If any person fails without reasonable cause or refuses -

a. To produce to an inspector or any person authorized by him in this behalf any book or paper which is his duty under sub-section (1) or sub-section (2) to produce.

b. To furnish any information which is his duty under sub-section (2) to furnish.

c. To appear before the inspector personally when required to do so under sub-section (4) or to answer any question which is put to him by the inspector in pursuance of that sub-section, or

d. To sign the notes of any examination referred to in sub-sec.(7),

He shall be punishable with imprisonment for a term which may extend to six months and with fine which shall not be less than twenty five thousand rupees but which may extend to one lakh rupees, and also with a further fine which may extend to two thousand rupees for every day after the first during which the failure or refusal continues.

(9) The officers of the Central Government, State Government, Police or Statutory Authority shall provide assistance to the inspector for the purpose of inspection, inquiry or investigation, which the inspector may, with the prior approval of the Central Government, require.

(10) The Central Government may enter into an agreement with the Government of a foreign State for reciprocal arrangements to assist in any inspection, inquiry or investigation under this Act or under the corresponding law in force in that State and may, by notification, render the application of this Chapter in relation to a foreign State with which reciprocal arrangements have been made subject to such modifications, exceptions, conditions and qualifications as may be deemed expedient for implementing the agreement with that State.

(11) Notwithstanding anything contained in this Act or in the Code of Criminal Procedure, 1973 (2 of 1974) if, in the course of an investigation into the affairs of the company, an application is made to the competent court in India by the inspector stating that evidence is, or may be, available in country or place outside India, such court may issue a letter of request to a court or an authority in such country or place, competent to deal with such request, to examine

orally, or otherwise, any person, supposed to be acquainted with the facts and circumstances of the case, to record his statement made in the course of such examination and also to require such person or any other person to produce any document or thing, which may be in his possession pertaining to the case, and to forward all the evidence so taken or collected or the authenticated copies thereof or the things so collected to the court in India which had issued such letter of request:

Provided that the letter of request shall be transmitted in such manner as the Central Government may specify in this behalf:

Provided further that every statement recorded or document or thing received under this sub-section shall be deemed to be the evidence collected during the course of investigation.

(12) Upon receipt of a letter of request from a court or an authority in a country or place outside India, competent to issue such letter in that country or place for the examination of any person or production of any document or thing in relation to affairs of a company under investigation in that country or place, the Central Government may, if it thinks fit, forward such letter of request to the court concerned, which shall thereupon summon the person before it and record his statement or cause any document or thing to be produced, or send the letter to any inspector for investigation, who shall thereupon investigate into the affairs of company in the same manner as the affairs of a company are investigated under this Act and the inspector shall submit the report to such court within

thirty days or such extended time as the court may allow for further action:

Provided that the evidence taken or collected under this sub-section or authenticated copies thereof or the things so collected shall be forwarded by the court, to the Central Government for transmission, in such manner as the Central Government may deem fit, to the court or the authority in country or place outside India which had issued the letter of request.

Protection of employees during investigation (Sec.218)

(1) Not withstanding anything contained in any other law for the time being in force, if-

a. During the course of any investigation of the affairs and other matters of or relating to a company, other body corporate or person under Section 210, Section 212, Section 213 or Section 219 or of the membership and other matters of or relating to a company, or the ownership of shares in or debentures of a company or body corporate, or the affairs and other matters of or relating to a company, other body corporate or person, under Section 216; or

b. During the pendency of any proceeding against any person concerned in the conduct and management of the affairs of a company under Chapter XVI,

Such company, other body corporate or person proposes -

i. To discharge or suspend any employee; or

ii. To punish him, whether by dismissal, removal, reduction in rank or otherwise; or

iii. To change the terms of employment to his disadvantage,

The company, other body corporate or person, as the case may be, shall obtain approval of the Tribunal of the action proposed against the employee and if the Tribunal has any objection to the action proposed, it shall send by post notice thereof in writing to the company, other body corporate or person concerned.

(2) If the company, other body corporate or person concerned does not receive within thirty days of making of application under sub-section (1), the approval of the Tribunal, then and only then, the company, other body corporate or person concerned may proceed to take against the employee, the action proposed.

(3) If the company, other body corporate or person concerned is dissatisfied with the objection raised by the Tribunal, it may, within a period of thirty days of the receipt of the notice of the objection, prefer an appeal to the Appellate Tribunal in such manner and on payment of such fees as may be prescribed.

(4) The decision of the Appellate Tribunal on such appeal shall be final and binding on the Tribunal and on the company, other body corporate or person concerned.

(5) For the removal of doubts, it is hereby declared that the provisions of this section shall have effect without prejudice to the provisions of any other law for the time being in force.

Power of inspector to conduct investigation into affairs of related companies, etc. (Sec.219)

If an inspector appointed under Section 210 or Section 212 or Section 213 to investigate into the affairs of a company considers it necessary for the purposes of the investigation, to investigate also the affairs of -

a. Any other body corporate which is, or has at any relevant time been the company's subsidiary company or holding company, or a subsidiary company of its holding company.

b. Any other body corporate which is, or has at any relevant time been managed by any person as managing director or as manager, who is, or was, at the relevant time, the managing director or the manager of the company.

c. Any other body corporate whose Board of Directors comprises nominees of the company or is accustomed to act in accordance with the directions or instructions of the company or any of its directors; or

d. Any person who is or has at any relevant time been the company's managing director or manager or employee,

He shall, subject to the prior approval of the Central Government, investigate into and report on the affairs of the other body corporate or of the managing director or manager, in so far as he considers that the results of his investigation are relevant to the investigation of the affairs of the company for which he is appointed.

Seizure of documents by inspector (Sec.220)

(1) Where in the course of an investigation under this Chapter, the inspector has reasonable grounds to believe that the books and papers of, or relating to, any company or other body corporate or managing director or manager of such company are likely to be destroyed, mutilated, altered, falsified or secreted, the inspector may-

a. Enter, with such assistance as may be required, the place or places where such books and papers are kept in such manner as may be required, and

b. Seize books and papers as he considered necessary after allowing the company to take copies of, or extracts from, such books and papers as its cost for the purpose of his investigation.

(2) The inspector shall keep in his custody the books and papers seized under this section for such a period not later than the conclusion of the investigation as he considers necessary and thereafter shall return the same to the company or the other body corporate, or, as the case may be, to the managing director or the manager or any other person from whose custody or power they were seized:

Provided that the inspector may, before returning such books and papers as aforesaid, take copies of, or extracts from them or place identification marks on them or any part thereof or deal with the same in such manner as he considers necessary.

(3) The provisions of the Code of Criminal Procedure, 1973 (2 of 1974), relating to searches or seizures shall apply mutatis mutandis to every search or seizure made under this section.

Freezing of assets of company on inquiry and Investigation (Sec.221)

(*1*) Where it appears to the Tribunal, on a reference made to it by the Central Government or in connection with any inquiry or investigation into the affairs of a company under this Chapter or on any complaint made by such number of members as specified under sub-section (*1*) of section 244 or a creditor having one lakh amount outstanding against the company or any other person having a reasonable ground to believe that the removal, transfer or disposal of funds, assets, properties of the company is likely to take place in a manner that is prejudicial to the interests of the company or its shareholders or creditors or in public interest, it may by order direct that such transfer, removal or disposal shall not take place during such period not exceeding three years as may be specified in the order or may take place subject to such conditions and restrictions as the Tribunal may deem fit.

(2) In case of any removal, transfer or disposal of funds, assets, or properties of the company in contravention of the order of the Tribunal under sub-section (*1*), the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees, or with both.

Imprisonment of restrictions upon Securities (Sec.222)

(*1*) Where it appears to the Tribunal, in connection with any investigation under section 216 or on a complaint made by any person in this behalf, that there is good reason to find out the relevant facts about any securities issued or to be issued by a company and the Tribunal is of the opinion that such facts cannot be found out unless certain restrictions, as it may deem fit, are imposed, the Tribunal may, by order, direct that the securities shall be subject to such restrictions as it may deem fit for such period not exceeding three years as may be specified in the order.

(*2*) Where securities in any company are issued or transferred or acted upon in contravention of an order of the Tribunal under sub-section (*1*), the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees, or with both.

Inspector's report (Sec.223)

(*1*) An inspector appointed under this Chapter may, and if so directed by the Central Government shall, submit interim reports to that Government, and on the conclusion of the investigation, shall submit a final report to the Central Government.

(*2*) Every report made under sub-section (*1*) shall be in writing or printed as the Central Government may direct.

(*3*) A copy of the report made under sub-section (*1*) may be obtained [by members, creditors or any other person whose interest is likely to be affected] making an application in this regard to the Central Government.

(*4*) The report of any inspector appointed under this Chapter shall be authenticated either:

(*a*) by the seal, if any, of the company whose affairs have been investigated; or

(*b*) by a certificate of a public officer having the custody of the report, as provided under section 76 of the Indian Evidence Act, 1872 (1 of 1872),

and such report shall be admissible in any legal proceeding as evidence in relation to any matter contained in the report.

(*5*) Nothing in this section shall apply to the report referred to in Section 212.

Actions to be taken in pursuance of inspector's report (Sec.224)

(*1*) If, from an inspector's report, made under Section 223, it appears to the Central Government that any person has, in relation to the company or in relation to any other body corporate or other person whose affairs have been investigated under this Chapter been guilty of any offence for which he is criminally liable, the Central Government may prosecute such person for the offence and it shall be the duty of all officers and other employees of the company or body corporate to give the Central Government the necessary assistance in connection with the prosecution.

(*2*) If any company or other body corporate is liable to be wound up under this Act and it appears to the Central Government from any such report made under Section 223 that it is expedient so to do by reason of any such circumstances as are referred to in Section 213, the Central Government may, unless the company or body corporate is already being wound up by the Tribunal, cause to be presented to the Tribunal by any person authorised by the Central Government in this behalf:

(*a*) a petition for the winding up of the company or body corporate on the ground that it is just and equitable that it should be wound up;

(*b*) an application under section 241; or

(*c*) both.

(*3*) If from any such report as aforesaid, it appears to the Central Government that proceedings ought, in the public interest, to be brought by the company or any body corporate whose affairs have been investigated under this Chapter:

(*a*) for the recovery of damages in respect of any fraud, misfeasance or other misconduct in connection with the promotion or formation, or the management of the affairs, of such company or body corporate; or

(*b*) for the recovery of any property of such company or body corporate which has been misapplied or wrongfully retained,

the Central Government may itself bring proceedings for winding up in the name of such company or body corporate.

(*4*) The Central Government, shall be indemnified by such company or body corporate against any costs or expenses incurred by it in, or in connection with, any proceedings brought by virtue of sub-section (*3*).

(*5*) Where the report made by an inspector states that fraud has taken place in a company and due to such fraud any director, key managerial personnel, other officer of the company or any other person or entity, has taken undue advantage or benefit, whether in the form of any asset, property or cash or in any other manner, the Central Government may file an application before the Tribunal for appropriate orders with regard to disgorgement of such asset, property, or cash, as the case may be, and also for holding such director, key managerial personnel, officer or other person liable personally without any limitation of liability.

Expenses of Investigation (Sec.225)

(*1*) The expenses of, and incidental to, an investigation by an inspector appointed by the Central Government under this Chapter other than expenses of inspection under section 214 shall be defrayed in the first instance by the Central Government, but shall be reimbursed by the following persons to the extent mentioned below, namely:

(*a*) any person who is convicted on a prosecution instituted, or who is ordered to pay damages or restore any property in proceedings brought, under section 224, to the extent that he may in the same proceedings be ordered to pay the said expenses as may be specified by the court convicting such person, or ordering him to pay such damages or restore such property, as the case may be;

(*b*) any company or body corporate in whose name proceedings are brought as aforesaid, to the extent of the amount or value of any sums or property recovered by it as a result of such proceedings;

(*c*) unless, as a result of the investigation, a prosecution is instituted under section 224:

(*i*) any company, body corporate, managing director or manager dealt with by the report of the inspector; and

(*ii*) the applicants for the investigation, where the inspector was appointed under section 213,

to such extent as the Central Government may direct.

(*2*) Any amount for which a company or body corporate is liable under clause (*b*) of sub-section (*1*) shall be a first charge on the sums or property mentioned in that clause.

Voluntary winding up of company, etc., not to stop investigation proceedings (Sec.226)

An investigation under this Chapter may be initiated notwithstanding, and no such investigation shall be stopped or suspended by reason only of, the fact that:

(*a*) an application has been made under section 241;

(*b*) the company has passed a special resolution for voluntary winding up; or

(*c*) any other proceeding for the winding up of the company is pending before the Tribunal:

Provided that where a winding up order is passed by the Tribunal in a proceeding referred to in clause (*c*), the inspector shall inform the Tribunal about the pendency of the investigation proceedings before him and the Tribunal shall pass such order as it may deem fit:

Provided further that nothing in the winding up order shall absolve any director or other employee of the company from participating in the proceedings before the inspector or any liability as a result of the finding by the inspector.

Legal advisers and bankers not to disclose certain information (Sec.227)

Nothing in this Chapter shall require the disclosure to the Tribunal or to the Central Government or to the Registrar or to an inspector appointed by the Central Government:

(*a*) by a legal adviser, of any privileged communication made to him in that capacity, except as respects the name and address of his client; or

(*b*) by the bankers of any company, body corporate, or other person, of any information as to the affairs of any of their customers, other than such company, body corporate, or person.

Investigation, etc., of foreign companies (Sec.228)

The provisions of this Chapter shall apply *mutatis mutandis* to inspection, inquiry or investigation in relation to foreign companies.

Penalty for furnishing false statement, mutilation, destruction of documents (Sec.229)

Where a person who is required to provide an explanation or make a statement during the course of inspection, inquiry or investigation, or an officer or other employee of a company or other body corporate which is also under investigation:

(*a*) destroys, mutilates or falsifies, or conceals or tampers or unauthorisedly removes, or is a party to the destruction, mutilation or falsification or concealment or tampering or unauthorised removal of, documents relating to the property, assets or affairs of the company or the body corporate;

(*b*) makes, or is a party to the making of, a false entry in any document concerning the company or body corporate; or

(*c*) provides an explanation which is false or which he knows to be false,

he shall be punishable for fraud in the manner as provided in section 447.

Lecture – XVI

COMPROMISES, ARRANGEMENTS & AMALGAMATIONS OR MERGER

Chapter XV containing Sections 230 to 240 of the Companies Act, 2013 lays down the provisions relating to 'Compromises, Arrangements and Amalgamations'.

Lecture – XVII

PREVENTION OF OPPRESSION & MISMANAGEMENT (MAJORITY RULE AND PROTECTION OF MINORITY AGAINST OPPRESSION AND MISMANAGEMENT 'OR' MAJORITY POWERS AND MINORITY RIGHTS)

Chapter XVI containing Sections 241 to 246 of the Companies Act, 2013 lays down the provisions relating to 'Prevention of Oppression and Mismanagement. Section 241 provides for 'Application to Tribunal for relief in cases of oppression, etc. Section 242 Confers Powers on the Tribunal. Section 243 deals with Consequence of termination or modification of certain agreements. Section 244 provides for Right to apply to Tribunal for relief under Section 241 in case of oppression. Section 245 speaks about Class Action. Section 246 deals with Application of certain provisions to proceedings under Section 241 or Section 245.'

This Lecture covers –

1. Majority Rule or the Rule in *Foss vs. Harbottle.*
2. Protection of Minority Rights.

3. Prevention of Oppression and Mismanagement or Protection of Minority against Oppression and Mismanagement.

1. Majority Rule 'or'

The Rule in Foss v. Harbottle

Company is an artificial person created by law with perpetual existence and common seal. As it cannot act on its own, the administration of a company is vested in the Board of Directors and other Officials of the company, who are answerable and accountable to the share holders, who are real owners as they invest their money in the company by purchasing its shares. Issues relating to policy matters and other important matters of the company are decided in annual general meeting and extra-ordinary general meeting by majority opinion of the shareholders. In other words, the decision taken by the majority shareholders is binding on all.

Therefore, the fundamental principle of company law is that, the resolution/decision taken by the majority of shareholders is final and binding, unless there is some contrary provision in the charter of the company. This principle is popularly known as 'Majority Rule or Majority Decision.' According to Companies Act, paid up equity shareholding determines the voting right of the shareholders. Therefore, the decision of the majority shareholders in General Body Meeting is binding, if the majority of shareholders resolve it. Sometimes, such majority view may affect the interests of the remaining shareholders i.e. minority shareholders. In such situation, the question is whether the minority shareholders can protect their interest through court of law. The Company Law must protect the interests of the minority share holders from oppression and mismanagement by the majority share holders and it aims to maintain a harmony/balance between rights of the minority and majority share holders for a smooth and successful functioning of the company. This principle of Majority Rule was coined/created for the first time in the leading case, Foss vs. Harbottle, which is discussed below:

***Foss v. Harbottle*(1843) 2 Hare, 461: 67 ER 189 (Supermacy of the Majority** – In this case, the court upheld the majority view of the shareholders, though it affected the interests of

the minority shareholders. Therefore, the view laid down in this case is popularly known as 'The Rule in Foss vs. Harbottle'.

Facts of the case: Two minority shareholders in a company alleged that its directors were guilty of buying their own land for the company's use and paying themselves a price greater than its value. This act of the directors resulted in a loss to the company. The minority shareholders, therefore, decided to take an action for damages against the directors. The shareholders in general meeting by majority resolved not to take any action against the directors alleging that they were not responsible for the loss, which had been incurred. The Court dismissed the suit on the ground that the acts of directors were capable of confirmation by the majority of members and held that the proper plaintiff for wrongs done to the company is the company itself and not the minority shareholders. It further held that the company could act only through its majority shareholders.

The Court while delivering judgment, opined that the company alone would have the cause of action, and not the minority shareholders.

"It is an elementary principle of the law relating to joint stock companies that the court will not interfere with the internal management of the companies acting within their powers, and in fact it has no jurisdiction to do so."

The Court, inter-alia observed:

"The conduct with which the defendants are charged is an injury not to the plaintiffs exclusively; it is an injury to whole corporation. In such cases the rule is that the corporation should sue in its own name and in its corporate character. It is not a matter of course for any individual members of a corporation thus to assume to themselves the right of suing in the name of the corporation. In law the corporation and the aggregate of members of the corporation are not the same thing for purposes like this."

Lord Davey, while referring the rule of law, established in the case of *Foss vs. Harbottle in Burland vs. Earb,* (1902) AC 83 explained the principle of Majority Rule in the following terms –

'It is an elementary principle of the law relating to joint stock companies that the court will not interfere with the internal management of companies acting within their powers, and has no jurisdiction to do so.'

In ***Macdougall v. Gardiner*, (1875) 1 Ch. 13,** Mellish L.J. observed – 'If the thing complained of is the thing which in substance the majority of the company are enabled to do, or something has been done illegally which the majority of the company are entitled to do legally, there can be no use in having litigation about it, the ultimate aim of which is only that a meeting has to be called and then ultimately the majority gets its wishes'.

In short the rule laid down in above referred cases and specially in *Foss v. Harbottle*is that the will of the majority should prevail.

***Burland v. Earle* (1902) AC 83 –** In this case also the same rule has been applied and it has been held that if the directors invest the profits in certain ways instead of paying dividend to the shareholders, individual shareholders cannot approach the court for the redress, and only the company can bring an action.

The above rule laid down in Foss vs. Harbottle has been following in India in many cases. The Supreme Court in –

***Rajahmundry Electric Supply Corporation Ltd. v. Nageswara Rao* 1956) 26 Comp. Cas. 55 (SC)** observed that the courts would not in general, intervene at the instance of the shareholders, in the matters of internal administration, by its directors so long as they act within their powers.

It should be noted that the rule in Foss vs. Harbottle applies only where a corporate membership right is infringed and has no application where an individual right to membership is denied to a member.

In ***Edwards v. Halliwel*, (1950) 2All E.R. 1064l,** Jenkins LJ explained this rule in the following words:

'The rule in Foss vs. Harbottle comes to no more than this – First, the proper plaintiff in an action in respect of a wrong alleged to be done to a company or association of persons is prima facie

the company or the association of persons itself. Secondly, where the alleged wrong is a transaction which might be made binding on the company or association and on all its members by a simple majority of the members, no individual member of the company is allowed to maintain an action in respect of that matter.'

Again, in ***Pavlides v. Jensen(1956 Ch. 565)*** – minority share holders brought an action for damages against three directors and against the company itself alleging that they had been negligent in selling a mine owned by the company for £ 1,82,000 whereas its real value was £ 10,00,000. The Court held that the action was maintainable. Giving reasons for the decision the learned Judge observed, "It was open to the company, on the resolution of a majority of the share holders to sell the mine at a price decided by the company by a vote of majority to decide that if the directors by their negligence or error of judgment had sold the company's mine at an under-value, proceedings should not be taken against the directors.'

In ***Gray v. Lewis (1873) 8 Ch. 1035 (CA)*** – it was held that a company is a *persona at law*, therefore the action is vested in it and cannot be brought by individual share holder. Where there is a corporate body capable of filing a suit for itself to recover property either from its directors or officers or from any other person, that corporate body is the only proper plaintiff to sue and none else.

The Supreme Court of America affirmed the principle laid down in ***Foss v. Harbottle in Mc. Candless v. Furland (296 US 140 (157)*** – Justice Cardozo in this case held that the erring directors can get themselves absolved from their liability provided they can muster the support of majority share holders.

In ***Stein v. Blacke***, share holders who held 50 percent of company's shares sued the director alleging that he had misappropriated the assets of the company. The Court dismissed the petition and held that it was only the company which had a right to sue director and not the share holder because the loss caused due to alleged misappropriation was to the company and not any particular shareholder.

In India, the importance of the majority power has been recognized in ***Bhajekar v. Shinkar (Air 1934 Bom. 243)*** – in this case, the directors of a company resolved to appoint a company as its managing agents. The appointment was confirm at two general meetings of the company despite objections from certain share holders. Thereupon, the dissenting share holders who were in minority brought action to restrain the managing agents from acting. Their argument was that the appointee managing agents were a dummy company and it was not in the company's interest to appoint them. The Court ordered a general meeting to be held under the supervision of a chairman appointed by it. The chairman put a resolution to the effect 'whether the company is willing to maintain the suit and proceed with it'. The resolution was lost. Under these circumstances Court held, 'it is difficult to see how a few share holders who represent a minority are entitled to maintain the suit and ask the Court to interfere on the question as to who should be the managing agents of the company'. The action therefore, failed.

1. Illegal or Ultravires Act.
2. Fraud against Minority.
3. Acts requiring Special Majority are ratified in Simple Majority.
4. Infringement or Violation of Individual Membership Rights.
5. Wrongdoers in Control.
6. Where there is an oppression of Minority or Mismanagement.

Exceptions to the Rule: The Rule is Foss vs. Harbottle does not apply in the following cases.

1. Illegal or Ultravires Act: The word 'Ultra' means "beyond" and the word 'Vires' means "Power". Hence, the expression 'Ultra Vires' means "Beyond the Power". All the officials viz. managerial personnel, directors and share holders are expected/ supposed to act within the powers conferred on them by the Memorandum or Article of Association. If they act beyond the power conferred, it amounts to 'ultra vires', which is not binding/ unenforceable/illegal. Therefore, every shareholder has a right to

bring an action against the company and its officers from an illegal or ultra vires acts.

***Bharat InsuanceLtd. v. Kanhayalal*:** The plaintiff in this case was a shareholder of the defendant insurance company. The plaintiff complained that several investments have been made by the company without adequate securities, contrary to the provisions of the Memorandum. Held that the suit is maintainable on the ground that the directors' act ultra vires.

The English Chancery Court in ***Smith v. Croft (No.II) (1987) 3 All ER 909 (Ch.D),*** held that where the majority of the share holders have by a resolution agreed that the over-payment made to the directors should not be recovered from them, the suit filed by the minority share holders against the majority decision will not be maintainable.

2. Fraud Against Minority: The rule does not apply if majority shareholders commit fraud to oppress the minority shareholders.

In ***Greenhalgh v. Arderone Cinemas Ltd. (1950) 2 All ER 1120)*** – Evershed MR observed that 'a special resolution would be liable to be impeached if the effect of it were to discriminate between the majority share holders and minority share holders so as to give to the former an advantage of which the latter were deprived.'

In ***Cook v. Deeks (1916) 1 AC 554 PC*** – In this case three directors of a railway construction company obtained a contract in their own name to construct a railway line. The directors had used their position as directors to obtain the contract and it obviously amounted to breach of trust by them who then used their voting powers to pass a resolution of the company declaring that the company was not interested in the contract. It was held that the directors must account to the company for the profits they made, apparently at the expense of minority.

In ***Allen v. Gold Reefs of West Africa (1900) 1 Ch 656 (671)*** – Lindley, MR reiterated the rule that majority powers must be exercised *bona fide* in good faith for the benefit of the company

as a whole. If they have not been so exercised there is a 'fraud on the minority'.

In ***Brown v. British Abrasive Wheel Co. (1919) 1 Ch 290)*** – a large majority representing 98% of the share holders wished to buy up the minority with a view to extending the capital. The minority refused to sell, and the majority then passed special resolutions altering the articles so as to enable nine-tenths of the share holders to buy out any other share holders. Held, the alteration of the articles could be restrained; the majority could not be allowed to expropriate the interests of minority share holders.

3. Acts requiring Special Majority are ratified in Simple Majority: Some decisions are valid by simple majority, while others are valid by special i.e. 3/4th majority. If a decision is taken by simple majority instead of special majority, such decision is not valid and binding. Hence, the rule in Foss v. Harbottle is not applicable.

In ***Dhakeswari Cotton Mills Ltd. v Nil Kamal Chakarvarty (AIR 1937 Cal. 645)*** the Calcutta High Court held that where voting on a resolution takes place by show of hands, a declaration by the chairman that a resolution has or has not been passed is conclusive only if he does not find by his declaration the figures for or against the resolution. But where the chairman finds the figures and erroneously in point of law holds that resolution has been duly passed, the resolution cannot be said to have been passed according to the law and therefore liable to be set aside.

4. Infringement or Violation of Individual Membership Right: If the majority rule infringes the personal or individual membership rights of a shareholder from minority shareholders the rule does not apply. The majority rule prevails only in respect of corporate membership right and not where any personal right of the individual member has been infringed. Thus, for example, right to receive dividend is a corporate membership right as it cannot be exercised unless dividends are declared by the company at the general meeting. But a right to transfer the shares held in the company or right to vote is a personal right of the individual member.

In*Kraus v. Lloyd Property Ltd. (1965) VR 232)* – In this case, the director refused to retire in accordance with the articles and wrongfully continued in office, the plaintiff share holder was entitled to bring an action on the ground that 'the individual rights of the plaintiff as a member have been invaded' by the erring director.

In *NagappaChetti v. Madras Race Club (1949) 1 MLJ 662 (667)* - the High Court of Madras ruled that a share holder is entitled to enforce his individual rights against the company such as right to vote, the right to have vote recorded, or his right to contest for directorship of a company at an election.

5. Wrongdoers in Control: Sometimes an obvious wrong may have been to the company, but the controlling share holders would not permit an action to be brought against the wrong doer. In such cases, to safeguard the interest of the company, any member or members may bring an action in the name of company.

In *Wallersteiner v. Moir (No.2) (1975) 1 All ER 849 (CA)* – it has been held that where wrongdoers themselves control the company, an action can be brought on behalf of the company by the minority share holders on the footing that they are its representatives to obtain redress on its behalf.

6. Where there is an oppression of Minority or Mismanagement: Section 241 of the Companies Act, 2013 (Corresponding to Sections 397 and 398 of the Companies Act, 1956) provide for the provisions relating to prevention of oppression and mismanagement. In this case the rule in *Foss v. Harbottle* does not apply. A remedy under Section 241 is, however, only available to members who apply to Tribunal in their capacity as members and the matters complained of must relate to the affairs of the company.

In *KanikaMukherji v. RameshwarDayal Dubey (1966) 1 comp. LJU 65 Cal.*Justice Sinha of the High Court of Calcutta observed that relief against oppression by majority shall be available to minority share holders provided it relates to the companies affairs but if it is directed towards a third person, it shall not be available. It was further held in this case that 'inefficient management will not

amount to oppression, though it may amount to mismanagement so as to come under Section 398 of the Companies Act, 1956 (now Section 241 of the 2013 Act)'.

2. Protection of Minority Rights

The Companies Act, 1956 attempts to maintain a proper balance between the rights of the majority and the minority shareholders. It admits in principle the rule of majority but limits it at the same time by a number of well-defined minority rights, thus protecting the minority shareholders.

Palmer has rightly stated that a proper balance of the rights of majority and minority shareholders is essential for the smooth functioning of the company. Thus the minority shareholders are required to be protected from the unjust or unfair conduct of the majority. The minority shareholders are protected under –

1. The general law; and

2. The Companies Act.

1. The General Law: Refer ... exceptions to the Rule in *Foss v. Harbottle*as above.

2. The Companies Act, 2013: Individual membership rights and minority rights conferred on shareholders by the Companies Act, 1956 have protected the interest of minority shareholders to a large extent. These rights relate to –

i. The variation of class rights (Sec.48).

ii. Schemes of reconstruction and amalgamation (Sec.230).

iii. The right to a remedy under Sec.241 as an alternative to the winding up of the Company.

iv. The right to remedy under Sec.241 to the winding up of the Company; and

v. The right to apply to the Central Government under Sec.210 of the Companies Act, 2013.

i. Variation of Class Rights: Where the share capital of a company is divided into different classes of shares, the rights attached

to the shares of any class can be varied as provided in the memorandum or articles of the company with the consent of three-fourth majority of the shareholders of that class. Where this is done and the rights are varied by the requisite majority vote, the holders of not less than 10 per cent of the issued shares of that class who had not assented to the variation may apply to the court for the cancellation of the variation under the Act.

ii. Scheme of reconstruction and amalgamation: Section 230 of the Companies Act, 2013 (Corresponding to Sec.391 of the Company Act, 1956) provides for scheme of reconstruction and gives protection to minorities.

iii. Prevention of oppression and mismanagement: A member who complaints that the affairs of the company are being conducted in a manner prejudicial to public interest or in a manner oppressive to some of the members, including himself may apply to Court/Tribunal, by petition under Section 241 of the Act. He may also apply for appropriate relief on the ground of mismanagement of the company under Section 242 of the Companies Act, 2013.

But, in order to attract the provisions of Sec.397 of the Companies Act, 1956 it must be shown that the conduct, affairs of a company by the majority shareholders was oppressive to the minority members and this requires that events have to be considered not in isolation but as part of a consecutive story. There must be continuous acts on the part of majority shareholders, continuing up to the date of petition, showing that the affairs of the company were being conducted in a manner oppressive to some part of the members.

If the court is of opinion that the affairs of the company are being conducted in a manner prejudicial to public interest or in a manner oppressive to any member or members and that a winding up would be unfair to those members, but that fact would justify a winding up order, the court may make an order regulating the conduct of the company's affairs.

iv. The right to a remedy under Sec.241 to the winding up of the Company: If the Court is of opinion that the affairs of the

company are being conducted in a manner prejudicial to public interest or in a manner prejudicial to public interest or in a manner oppressive to any member or members and that a winding up would be unfair to those members, but that fact would justify a winding up order, the court may make an order regulating the conduct of the company's affairs.

v. The right to apply to the Central Government under Sec.210: (1) Where the Central Government is of the opinion that it is necessary to investigate into the affairs of a company –

a. On the receipt of a report of the Registrar or inspector under Sec.208.

b. On intimation of a special resolution passed by a company that the affairs of the company ought to be investigated; or

c. In public interest,

It may order an investigation into the affairs of the company.

(2) Where an order is passed by a Court or the Tribunal in any proceedings before it that the affairs of a company ought to be investigated, the Central Government shall order an investigation into the affairs of that company.

(3) For the purposes of this section, the Central Government may appoint one or more persons as inspectors to investigate into the affairs of the company and to report thereon in such manner as the Central Government may direct.

3. Prevention of Oppression and Mismanagement

Chapter XVI containing Section 241 to 246 of the Companies Act, 2013 (Corresponding to Chapter VI of Part VI containing Sections 397 to 409 of the Companies Act, 1956) lays down the provisions relating to 'Prevention of Oppression and Mismanagement'.Section 241 provides for 'Application to Tribunal for relief in cases of oppression, etc. Section 242 Confers Powers on the Tribunal. Section 243 deals with Consequence of termination or modification of certain agreements. Section 244 provides for Right to apply to Tribunal for relief under Section 241 in case of

oppression. Section 245 speaks about Class Action. Section 246 deals with Application of certain provisions to proceedings under Section 241 or Section 245.'

The words 'Oppression' and 'Mismanagement' are not defined in the Companies Act. For the purpose of the Company Law, its meaning was explained in *Elder* v. *Elder and Watson Ltd.* (1952) SLT 112. The word oppression in broad generic sense means 'any act exercised in a manner burdensome, harsh and wrongful. It lacks fair dealings in company affairs, which prejudice some members. E.g.: An attempt to force new and more risky objects against the willing of minority shareholders.

Oppression – Meaning: The word 'Oppression' is a chameleonic word. It changes its colour content and form from time to time, place to place event to event depending on the circumstances of the case. The word oppression literally means 'burdensome or unbearable or harsh.'

There is no definition of the term 'oppression' in the Companies Act. It is to be decided on the facts of each case whether there exists oppression or not. The conduct of the majority (or minority) shareholders may be treated as oppressive if it involves a visible departure from the standards of fair dealing and a violation of the conditions of fair play on which every shareholder who entrusts money to the company is entitled to rely.

Osborn's dictionary: 'Oppression is a misdemeanour committed by majority shareholders, who under colour of their majority power, wrongfully inflict upon the minority shareholder or minority shareholders any harm of injury.'

Lord Cooper explained the meaning of 'oppression' in case '*Elder* v. *Watson Ltd.* 1952' in the following words:

'The essence of the matter seems to be that the conduct complained of should at the lowest involve a visible departure from the standards of fair dealing, and a violation of the conditions of fair dealing, and a violation of the conditions of fair play on which every shareholder who entrusts his money to the company is entitled to rely.'

The Supreme Court in ***Daleant Carrington Investment (P) Ltd. v. P.K.Prathapan (2004) 4 Comp. LJ 1 (S.C),*** held that increase of share capital of a company for the sole purpose of gaining control of the company, where the majority share holder is reduced to minority, would *mala fide* and would amount to oppression. The director holds a fiduciary position and could not on his own issue shares to himself. In such cases the oppressor would not be given an opportunity t buy out the oppressed.

Prevention of oppression (Sec.241(1)): (*1*) Any member of a company who complains that:

(*a*) the affairs of the company have been or are being conducted in a manner prejudicial to public interest or in a manner prejudicial or oppressive to him or any other member or members or in a manner prejudicial to the interests of the company; or

(*b*) the material change, not being a change brought about by, or in the interests of, any creditors, including debenture holders or any class of shareholders of the company, has taken place in the management or control of the company, whether by an alteration in the Board of Directors, or manager, or in the ownership of the company's shares, or if it has no share capital, in its membership, or in any other manner whatsoever, and that by reason of such change, it is likely that the affairs of the company will be conducted in a manner prejudicial to its interests or its members or any class of members,

may apply to the Tribunal, provided such member has a right to apply under section 244, for an order under this Chapter.

Thus the complaint regarding 'oppression' can be made on the ground of public interest and interest of the company. Further, complaint before the Tribunal can also be made where the interest of creditors or debenture holders or class of share holders is adversely appealed by virtue of alteration in Board in Directors or in ownership in the company's shares.

Complaint against oppression : who have right to apply (Sec.244): According to this section the following members shall have right to complain –

a. In the case of a company having a share capital, not less than one hundred members of the company or not less than one tenth of the total number of its members, which over is less on any member or members holding not less than one tenth of issued share capital of the company:

Provided that the applicant or applicants has or have paid all calls and after sums due on his or their shares.

b. In case of a company not having a share capital, not less than one fifth of the total member of its member.

However, Tribunal may waive all may of the aforesaid requirements.

If this context if the shares of as company are held jointly by two or more persons, it shall be counted as one member.

'Consent in writing to be given by the members for the purpose of filing complaint before the Tribunal.'

Oppression – When an application entertained by the Tribunal (Sec.242(1)): Wherein application to the Tribunal for relief in cases of oppression etc. is made under Section 241 of the Companies Act, 2013 and the Tribunal is of the opinion that –

i. The company's affairs have been or are being conducted in a manner prejudicial or oppressive to any member or members or prejudicial to public interest or in a manner prejudicial to the interests of the company, and

ii. That to wind up the company would unfairly prejudice such member or members, but that otherwise the facts would justify the making of a winding up order on the ground that it was just and equitable that the company should be wound up.

On existence of the aforesaid twin conditions and with a view to bringing to an end the matters complained i.e. mismanagement oppression, the Tribunal may make such order as it thinks fit.

Powers of Tribunal (Sec.242(2)): On fulfilment of conditions contemplated in Section 242(2) of the Companies Act, 2013 the Tribunal may pass order in respect of that –

a. Forms of Regulation: The regulation of conduct of affairs of the company in future.

b. Purchase of shares: The purchase of shares or interests of any members of the company by other members thereof or by the company.

c. Reduction of share capital: In the case of the purchases of its shares by the company as aforesaid, the consequent reduction of its share capital.

d. Transfer/allotment of shares: Restriction on the transfer or allotment of the shares of the company.

e. Termination/modification of agreement: The termination, setting aside or modification of any agreement, howsoever arrived at between the company and the managing director, any other director or manager, upon such terms and conditions as may, in the opinion of the Tribunal, be just and equitable in the circumstances of the case.

f. Termination etc.of other agreement: The termination, setting aside or modification of any agreement between the company and any person other than those referred to the clause (e):

Provided that no such agreement shall be terminated set-aside or modified except after due notice and other obtaining the consent of the party concerned.

g. Transfer delivery of goods property: The setting aside of any transfer, delivery of goods, payment, execution or other act relating to property made or done by or against the company within three months before the date of application under this section which would, if made or done by or against individual be deemed in his insolvency to be a fraudulent preference.

h. Removal of Managerial person: Removal of managing director, manager or any of the directors of the company.

i. Undue gain and its recovery: Recovery of undue gain by the key managerial person.

j. Appointment of Managerial persons: The manner in which the key managerial persons may be appointed, subsequent to an order removing the existing managerial persons.

k. Number of Managerial persons: Appointment of such member of persons of directors, who may be required by the Tribunal to report to the Tribunal on such matters as the Tribunal may direct.

l. Power to impose cost: Imposition of costs as may be deemed fit by the Tribunal.

m. Making of Just and Equitable provisions: Any other matter for which in the opinion of the Tribunal, it is just and equitable that provision should be made.

It is submitted that by virtue of Section 242(2) of the Companies Act, 2013 the Tribunal has power to regulate and control the affairs of the company on just and equitable ground.

However, a certified copy of the order of the Tribunal shall be filed by the company in question with the Registrar of Companies within thirty days of the order of the Tribunal. A responsibility is casted on tribunal to record its decision at the conclusion of hearing, specifically as to whether or not the respondent is a fit and proper person to hold the office of director or any other office connected with the conduct and management of any company.

Mismanagement – Meaning: Mismanagement of the company means the affairs of the company are being conducted in a manner prejudicial to public interest or in a manner prejudicial to the interests of the company. It is also said to be mismanagement, where a material change has taken place in the management or control of the company whether by an alteration in its Board of Directors or manager or in the ownership of the company's shares, or if it has no share capital in its membership, or in any other manner whatsoever, and that by reason of such change, it is likely that the affairs of the company will be conducted in a manner prejudicial to public interest or in a manner prejudicial to the interests of the company.

The administration of a company is vested in a body called 'Board of Directors' and other officials, who are answerable and accountable to the shareholders. The decision taken by the majority shareholders in the General Body meeting is final and binding even though it affects the interests of the minority shareholder owing to oppression and mismanagement by the Directors, who are found

successful in securing majority rule in their favour. In such situations it is necessary to protect the interests of the minority shareholders.

What Constitutes Mismanagement?: The present Companies Act, 2013 does not provide definition of the expression 'mismanagement'. However, it connotes that when the affairs of the company are being conducted in a manner prejudicial to the interest of the company or the members or against the public interest, it amount to 'mismanagement'.

Conditions for relief: Where in

i. The affairs of company is being conducted in a manner which is prejudicial to public interest, interest of any member or members or in the company's interest, the affairs in question may be oppressive in whatsoever manner.

ii. The natural charge brought in the bound of directors or in ownership of the company's shares prejudicial affecting the interest of creditors, debenture holders or class of share holders.

By virtue of Section 242(1) of the Company Act, 2013 on any application made under section 141, the Tribunal is of the opinion –

(a) that the company's affairs have been or are being conducted in a manner prejudicial or oppressive to any member or members or prejudicial to public interest or in a manner prejudicial to the interests of the company, and

Who can complain of mismanagement?: Section 399 of the Companies Act, 1956 (Corresponding Section 244 of the Companies Act, 2013) deals with the right to make complaint regarding oppression and mismanagement in the affairs of company under Sections 397 and 398 (Corresponding Section 244 of the Companies Act, 2013) respectively.

In case of oppression and mismanagement, and member of a company under Section 397 or 398 (Corresponding of Section 241 of the Companies Act, 2013) may apply to the Court for granting appropriate relief. The following members of a company shall have the right to apply under Section 397 or 398 of the Companies Act,

1956 (Corresponding Sections 241 and 242 of the Companies Act, 2013 respectively):

i. In case of a company having a share capital, not less than one hundred members of the company, or not less than one tenth of the total number of its members, whichever is less, or any member or members holding not less than one tenth of the issued share capital of the company.

ii. In the case of a company not having a share capital, not less than one fifth of the total number of its members.

According to Section 399(3) of the Companies Act, 1956 (Corresponding Section 244) of the Companies Act, 2013) 'where any members of a company are entitled to make an application, any one or more of them having obtained the consent in writing of the rest, may make the application on behalf and for the benefit of all others.'

However, the holder of a general power of Attorney for and on behalf of a share holder can validly give consent to a petition under Section 397 or 398 of the Companies Act.

The Supreme Court in ***Shanti Prasad v. Kalinga Tubes Ltd. (AIR 1965 SC 1535),*** observed the Section 398, i.e. prevention of mismanagement comes into play when there is actual mismanagement or apprehension of mismanagement of the affairs of the company. It may be contrasted with Section 397 (Corresponding Sections 241 of the Companies Act, 2013) which deals with the oppression to the minority share holders, whether there is prejudice to the company or not.

But, the Supreme Court in ***P.Punniah v. Jeypore Sugar Co. Ltd. (AIR 1994 SC 2258),*** held that Section 399 does not either expressly or by implication indicate that the consent to be accorded there under should be given by the member personally. Thus, a legal representative or a power of attorney holder on behalf of the deceased share holder or the principal can validly give consent to the petition under Section 397 or 398 of the Companies Act, 1956 (Corresponding Sections 241 and 242 of the Companies Act, 2013 respectively).

Further, Sections 399(4) of the Companies Act (Corresponding of Section 249 of the Companies Act, 2013) provides that the Central Government, if it is of opinion that circumstances exist which make it just and equitable to do, so, authorize any member or members of the company to apply to the Tribunal to get remedy under Section 397 or 398 of the Act. In such circumstances the requirement as to the consent of requisite number of members is exempted when the Central Government grants permission to apply under Section 397 or 398 of the Companies Act, 1956 (Corresponding Sections 241 and 242 of the Companies Act, 2013 respectively).

Distinction between Oppression and Mismanagement: In the preceding Companies Act, 1956, Section 397 of the Act dealt with relief against oppression whereas Section 398 was related to prevention of mismanagement. It is important to note that the relief available under the two sections differs in the following aspects:

1. In case of oppression under Section 397, there should have been facts to justify the making of an order for winding up, but no such facts were necessary in case of claiming relief against mismanagement under Section 398.
2. Under Section 397, the Tribunal by its order, prevents injustice being done to the member or members in capacity of member, but under Section 398, the Tribunal makes an order to prevent injustice being done to the interests of the company as a whole.
3. The provision of Section 398 was of a preventive nature whereas under Section 397, the Tribunal sought to end the oppression complained of by the petitioner.

However, in the Companies Act, 2013, the provisions of Sections 397 and 398 of the preceding Companies Act, 1956 have been brought together under a single section i.e. Section 241 which provides for application to Tribunals for relief in cases of oppression. There is no separate section for relief against mismanagement and an application against mismanagement in a company may be made to the Tribunal under the same section i.e. Section 241 of the Act.

Lecture – XVIII
REGISTERED VALUERS (Section 247)

Chapter XVII containing Section 247 provides for the valuation of companies assets viz. properties, stocks, shares, debentures, securities etc. by the registered valuers. This Chapter is not yet notified. It runs as follows –

Registered Valuers (Sec.247): (*1*) Where a valuation is required to be made in respect of any property, stocks, shares, debentures, securities or goodwill or any other assets (herein referred to as the assets) or net worth of a company or its liabilities under the provision of this Act, it shall be valued by a person having such qualifications and experience and registered as a valuer in such manner, on such terms and conditions as may be prescribed and appointed by the audit committee or in its absence by the Board of Directors of that company.

(*2*) The valuer appointed under sub-section (*1*) shall:

(*a*) make an impartial, true and fair valuation of any assets which may be required to be valued;

(*b*) exercise due diligence while performing the functions as valuer;

(*c*) make the valuation in accordance with such rules as may be prescribed; and

(*d*) not undertake valuation of any assets in which he has a direct or indirect

interest or becomes so interested at any time [during a period of three years prior to his appointment as valuer or three years after the valuation of assets was conducted by him].

(*3*) If a valuer contravenes the provisions of this section or the rules made thereunder, the valuer shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees:

Provided that if the valuer has contravened such provisions with the intention to defraud the company or its members, he shall be punishable with imprisonment for a term which may extend to

one year and with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

(*4*) Where a valuer has been convicted under sub-section (*3*), he shall be liable to:

(*i*) refund the remuneration received by him to the company; and

(*ii*) pay for damages to the company or to any other person for loss arising out of incorrect or misleading statements of particulars made in his report.

Lecture – XIX

REMOVAL OF NAMES FROM THE REGISTER OF COMPANIES (DISSOLUTION OF A COMPANY)

Chapter XVIII containing Sections 248 to 252 of Companies Act, 2013 lays down the provisions relating to 'Removal of Names from the Register of Companies'.

Lecture – XX
WINDING UP OF COMPANIES

Chapter XX containing Section 270 to 365 of the Companies Act, 2013 lays down the various provisions relating to winding up of companies.

Chapter XX containing Section 270 to 365 of the Companies Act, 2013 lay down the various provisions relating to winding up of companies.

Section 270 of Chapter XX provides for different modes of winding up of the companies. Sections 271 to 365 are sub-divided into four parts. Part-I containing Sections 271 to 303 lays down the provisions relating to 'winding up by the Tribunal'. Part-II containing Sections 304 to 323 lays down the provisions relating to 'Voluntary Winding up'. Part-III containing Sections 324 to 358 provides for the provisions applicable to every mode of winding up. Part-IV containing Sections 359 to 365 provides for the appointment of liquidator, his powers, functions etc.

Winding up or Liquidation: Meaning

The expression 'Winding up' or 'Liquidation' is a process by which the existence or life of a company is put to an end.' It is also termed as 'Liquidation'. Winding up or liquidation is a process by which the life of a company is ended and its properties are administered for the benefit of its members and creditors. The person appointed for administering the assets and liabilities is called 'Liquidator'. On liquidation, the company's name is deleted from the list of companies by the Registrar of Companies and the same is published in the Official Gazette.

When a business house, sole trading concern or partnership firm is closed due to excess of liabilities over assets, it is called 'insolvency'. It is called Bankruptcy in England. The proprietor or partner is called 'insolvent' (or bankrupt in England). If a company

(Private or Public Ltd.) is closed, it is called 'winding up or liquidation'.

Distinction between Insolvency and Winding up: Following are the notable points of distinction between Insolvency and Winding up.

Insolvency	Winding up
1. Only an individual can be adjudged as insolvent.	1. Only a company can be wound up.
2. Only a debtor can be adjudged as an insolvent.	2. A solvent company may be wound up.
3. Insolvency always results deficiency.	3. Winding up may end in surplus assets.
4. When a person is adjudged as insolvent he ceases to be a legal person.	4. Company continues to be a legal person until it is dissolved.
5. Assets vests with the Office Assignee.	5. Assets continue to be with the company but the administration is taken over by the liquidator.
6. When the insolvency proceedings are completed the insolvent will be discharged. That is to say free from all his debts. He again becomes a legal person.	6. There is no such discharge. When winding up has been completed the company will be killed, i.e. dissolved.
7. Any goods in the possession of an insolvent will be deemed to be his, until proved to be otherwise. This principle is known as reputed ownership.	7. The principle of reputed ownership does not apply.

Definition: Prof. Gower's Definition – Winding up of a company is a process whereby its life is ended and its property administered for the benefit of its creditors and members. An administrator, called liquidator, is appointed and he takes control of

the company, collects its assets, pays its debts and finally distributes and surplus among the members in accordance with their rights.

Pennington's Definition – Winding up is a process by which the management of a company's affairs is taken out of its directors hands, its assets are realised by a liquidator, and its debts are paid out of the proceeds of realisation and any balance remaining is returned to its members. At the end of the winding up the company will have no assets or liabilities, and will therefore be simply a formal step for it to be dissolved, that is, for its legal personality as a corporation to be brought to an end.

Object: The object of winding up is to save the creditors and members from further losses and indebtedness and equitable distribution of assets and liabilities among the creditors and members.

Modes or Kinds of winding up (Sec.270): Section 270 of the Companies Act, 2013 provides for the different modes/kind of winding up as stated below —

1. Winding up by the Tribunal (Sec. 271) and
2. Voluntary winding up (Sec.304).

Part I — Winding up by the Tribunal

Circumstances in which company may be wound up by Tribunal (Sec. 271): (*1*) A company may, on a petition under section 272, be wound up by the Tribunal:

(*a*) if the company has, by special resolution, resolved that the company be wound up by the Tribunal;

(*b*) if the company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality;

(*c*) if on an application made by the Registrar or any other person authorised by the Central Government by notification under this Act, the Tribunal is of the opinion that the affairs of the company have been conducted in a fraudulent manner or the company was formed for fraudulent and unlawful purpose or the persons concerned in the formation or management of its affairs have been guilty of fraud, misfeasance or misconduct in

connection therewith and that it is proper that the company be wound up;

(*d*) if the company has made a default in filing with the Registrar its financial statements or annual returns for immediately preceding five consecutive financial years; or

(*e*) if the Tribunal is of the opinion that it is just and equitable that the company should be wound up.

Petition for winding up (Sec. 272): (*1*) Subject to the provisions of this section, a petition to the Tribunal for the winding up of a company shall be presented by:

(*a*) the company;

(*b*) any contributory or contributories;

(*c*) all or any of the persons specified in clauses (*a*) and (*b*)

(*d*) the Registrar;

(*e*) any person authorised by the Central Government in that behalf; or

(*f*) in a case falling under clause (*b*) of Section 271, by the Central Government or a State Government.

a. The company (Sec. 439(1)(a): It has been noted above that the company may resolve by a special resolution to wind up the company. After such a resolution is passed the company may present a petition for winding up.

In ***Re Patiala Vanaspati Co. (AIR 1953 Pepsu 195),*** the petition for winding up of the company was made by the managing director. Rejecting the petition, the Court (now Tribunal) held that the resolution of the general meeting was necessary for the petition as the directors or managing director did not constitute the company for this purpose.

The English Court in ***Re Emmadart Ltd. (1979) 1 All ER 599),*** held that the general powers of the management of business delegated to the Board of Directors do not include the power to end the existence of a company. Therefore the approval of the general meeting through a special resolution was necessary for presenting a petition for winding up by the company.

In ***Central Bank of India v. Sukhani Mining Industries (1977) 47 Comp. Cas. 1 (Pat),*** it has been held that a creditor who is pursuing his ordinary remedy in a civil suit for recovery of his debt, can also make a petition for winding up under Section 271 of the Companies Act, 2013. The Tribunal may order the stay of his suit but cannot disqualify him from presenting a petition for winding up on that ground.

b. Any Contributory or Contributories (Sec.272(1)(b): A 'contributory' means, 'every person liable to contribute to the assets of a company in the event of its being wound up, and includes the holder of fully paid up share.'

A contributory shall be entitled to present petition for winding up notwithstanding that he may be the holder of fully paid up shares, or that the company may have no asset at all, or may have no surplus assets left for distribution among the shareholders after the satisfaction of its liabilities. A contributory shall be entitled to present a petition for winding up in any of the following situations:

a) When the number of members, in the case of a public company is reduced below seven, and in the case of a private company, below two (other than a One Person Company).

b) When the shares in respect of which he is a contributory either were originally allotted to him or have been held by him, and registered in his name, for at least six months during the 18 months immediately before the commencement of winding up, or have devolved on him through the death of a former holder.

c. All or any one of the persons specified in Clauses (a) and (b): A petition for the winding up of a company under Sec.272 may be presented by all or any of the parties, namely, the company, contributories specified in Sec.272(a), (b) and (c) whether together or separately.

d. The Registrar (Sec.272(3): The Registrar shall be entitled to present a petition for winding up under Section 271, except on the grounds specified in clause (a) of that section:

Provided that the Registrar shall obtain the previous sanction of the Central Government to the presentation of a petition:

Provided further that the Central Government shall not accord its sanction unless the company has been given a reasonable opportunity of making representations.

e. Any person authorised by the Central Government (Sec. 272(1)(e): The Central Government may authorise any person to present a petition for winding up a company.

f. The Central Government or State Government (Sec.272(1)(f): It provides that in a case falling under Clause (f) of Section 272, the winding up petition may be presented by the Central Government or a State Government. According to Section 272(f), a winding up petition may be filed if the company has acted against the interests of sovereignty and integrity of India, the security of State, friendly relations with foreign States, public order, decency or morality.

Commencement of Winding up (Sec.357): Section 357 of the Companies Act,2013 (Corresponding to Section 441 of the Companies Act, 1956) deals with 'Commencement of Winding up by Tribunal'. Where before the presentation of a petition for the winding up of a company by the Tribunal, a resolution has been passed by the company for voluntary winding up, the winding up of the company will be deemed to have commenced at the time of the passing of the resolution and unless the Tribunal on proof of fraud or mistake, thinks fit to direct otherwise all proceedings taken in the voluntary winding up shall be deemed to have been validly taken.

In any other case, the winding up of a company by the Tribunal shall be deemed to commence at the time of the presentation of the petition for the winding up. In all other cases (i.e. where the company has not previously passed a resolution for voluntary winding up), the winding up will be deemed to commence from the time of the presentation of the petition for the winding up.

The Tribunal may dismiss or allow the petition for winding up and also can adjourn its hearing or pass conditional order of winding up. In a case the Court (now Tribunal) ordered for winding up but stayed the operation of the order for six months so as to enable the company to pay the petitioner, if it could do so within this period and in case of failure the order was to come in force.

Advertisement of petition: Every petition for winding up a company shall be advertised 14 days before the hearing, stating the date on which the petition was presented and the names and addresses of petitioners.

Powers of Tribunal (Sec. 273): (*1*) The Tribunal may, on receipt of a petition for winding up under section 272 pass any of the following orders, namely:

(*a*) dismiss it, with or without costs;

(*b*) make any interim order as it thinks fit;

(*c*) appoint a provisional liquidator of the company till the making of a winding up order;

(*d*) make an order for the winding up of the company with or without costs; or

Any of such order shall be made by the Tribunal within 90 days from the date of presentation of the petition.

In case the Tribunal orders the appointment of a Provisional Liquidator, it has to give a notice to the company and afford a reasonable opportunity to it to make its representation before passing of such order, unless for special reasons to be recorded in writing, the Tribunal thinks it fit to dispense with such notice.

The Tribunal shall not refuse to make a winding up order on the ground only that the assets of the company have been mortgaged for an amount equal to or in excess of those assets, or that the company has no assets.

Where a petition is presented on the ground of just and equitable cause (i.e. under Section 271(1)(e) of the Companies Act, 2013) for winding up of a company, the Tribunal may refuse to make a winding up order, if it is of opinion that some other remedy is available to the petitioners and they are acting unreasonably in seeking to have the company would up instead of pursuing other remedy.

Consequences of winding up order: According to Section 277 of the Companies Act, 2013 (Corresponding to Section 444 of the Companies Act, 1956) the order of winding up shall be

communicated/intimated to the company liquidator, provisional liquidator and the registrar of companies. Once the Tribunal makes an order for the winding up of a company, its consequences date back to the commencement of winding up. The other consequences of winding up by the Tribunal are as follows:

1. Filing copy of the order: The petitioner and the company are required to file with the Registrar of Companies, a certified copy of the Tribunal order, within one month of the order. The Registrar will then notify in the official Gazette that such order has been made.

2. Notice of discharge to officers: The order for winding up shall be deemed to be notice of discharge to the officers and employees of the company, except when the business of the company is continued for the purpose of beneficial realization of assets.

It is worth nothing, here that where an employee is on a contract of service for a term which has not expired on the date of winding up, the order will operate as a wrongful discharge, and damages will be allowed as for breach of contract of service (*Reigate v. Union Manufacturing Co.* (1918) 1 KB 592).

3. Power of directors terminated: The powers of the Board of Directors are terminated and the same will now be exercised by the Official Liquidator.

4. Operation in favour of all creditors: The winding up order shall operate in favour of all the creditors and all the contributories of the company, as if such an order has been made on their joint petition.

5. Official Liquidator: The Official Liquidator, shall by virtue of his office become the liquidator of the company.

6. Future debts: Any debts payable at a future date, become immediately payable on the winding up order.

7. Period of limitation: For computing the period of limitation in respect of suits and applications on behalf of or in the name of a company which is being wound up by the Tribunal, the period between the date of making the application for winding up and the

date of the order of winding up (both inclusive) and a period of one year immediately following the date of the winding up order, should be excluded. This shall hold good irrespective of anything to the contrary contained in the Indian Limitation Act, 1908, or in any other law.

8. Stay of suits and proceedings: No suit or legal proceeding can be commenced against the company without the leave of the Tribunal. Similarly, if a suit is pending against the company at the date of winding of order, it shall not be proceeded, with the permission of the Tribunal.

But in respect of Coking Coal Mines (Nationalisation) Act, 1972 and Coal Mines (Nationalisation) Act, 1973, no proceedings can be taken under section 279 of the Companies Act so as to interfere with the performance of the functions assigned to Commissioner of payments under the aforesaid Acts.

9. Powers of Tribunal: The Tribunal which is winding up the company shall have full powers to entertain or dispose of any new or pending suit or proceeding by or against the company. Any suit or proceeding in any other Tribunal shall also be transferred to the Tribunal in which the winding up of the company is proceeding.

10. The liability is enforced by means of calls. A contributory who is a creditor of the company cannot set off his debt against his liability for calls. [In Re Law Car and General Insurance Corpn. (1912) 1 Ch. 405].

11. A transfer of shares in the Company, not being a transfer made to or with the sanction of the liquidator, and any alteration in the status of the members of the company, made after the commencement of the winding up, shall be void (Sec.334).

12. Where any company is being wound up by or subject to the supervision of the Tribunal, the creditors cannot proceed with any execution of the decrees against the estate or effects of the company, without leave of the Tribunal (Sec.335).

13. A secured creditor may either value his security and prove in the winding for the balance of his debt, or give up his security and prove for the whole amount.

14. On the appointment of a liquidator all the powers of the board of directors cease, except in so far as the committee of inspection, or if there is no such committee, the creditors in general meeting may sanction the continuance thereof.

15. When a company is being wound up a floating charge on the property of the company created within the 12 months of the winding up shall, unless it is proved that the company immediately after the creation of the charge was solvent, be invalid, except to the amount of any cash paid to the company at the time of the creation of charge, together with interest on that amount at the rate of 5% per annum (Sec.332).

Appeal from winding up order: An appeal from any order or decision given in the matter of winding up of a company by the Tribunal shall lie to the same Tribunal provided such an order finally decides the dispute between the parties, and it is not merely a formal or an interlocutory order. Such an order would not be an administrative order but it would be a judicial order. However, it is not necessary that a final order of winding up should satisfy the test of judgment within the meaning of clause 15 of the Letters Patent.

In ***Anil Kumar Sachdeva v. Four 'A' Asbestos (P) Ltd. (1980) 50 comp. Cas. 122 (Del),*** it has been held that consequent to the passing of a winding up order by the Tribunal, the powers of the directors cease but there are still certain residuary powers vested with them and they are entitled to appeal against the order of winding up and can also challenge the *ex parte* order of winding up.

Appointment of Provisional Liquidator (Sec.275): As provided by Section 275 of the Companies Act, 2013 after the presentation of the petition but before the winding up order, the Tribunal may appoint an Official Liquidator to be the provisional Liquidator for the company. The provisional Liquidator becomes the Official Liquidator as soon as the winding up order is passed. Before making such appointment, the Tribunal informs the company so as to enable it to make representation, if any. It has, however, been held by the Kerala High Court in *Re Brunton & Co. (1988) 63 Comp. Cas. 299 (Ker),* that where the Tribunal apprehends

that the company is likely to divert or misuse its property to the detriment of creditors and share holders, it may appoint a provisional Liquidator even without giving an opportunity to the company to make representation. But the Tribunal must record its reasons for doing so in writing.

The power of the Tribunal to appoint a provisional Liquidator is discretionary and is generally exercised when winding up of the company is more or less certain. In this context, Romilly, MR observed:

'Where there is no opposition to the winding up, I appoint a provisional Liquidator as a matter of course on the presentation of the petition. But where there is an opposition to it, I never do, because I might paralyze all the affairs of the company and afterwards refuse to make a winding up order at all.'

Experience has shown that appointment of provisional Liquidator has always remained as debatable issue because it may cause more evil than good, particularly in cases where a provisional liquidator is appointed on the presentation of winding up petition but an order of winding up is not ultimately passed. It may shake the confidence of the people in the company which may adversely affect its business, goodwill and reputation.

Dissolution of the Company: When the company is wound up by the order of the Tribunal, the liquidator may not be able to proceed with winding up process for lack of funds/assets or any other reason. If the Tribunal thinks just and reasonable passes an order of dissolution with effect from the date of the order, the existence of the company ceases to exist (comes to an end). A copy of the order shall be forwarded by the liquidator to the Registrar of Companies.

Effect of winding up order (Sec. 278): The order for the winding up of a company shall operate in favour of all the creditors and all contributories of the company as if it had been made out on the joint petition of creditors and contributories.

Part II — Voluntary winding up (Sections 304 to 323): Omitted by Insolvency and Bankruptcy Code, 2016 (Act 31 of 2016, w.e.f. 15-11-2016)

Lecture–XXI

LIQUIDATOR OR OFFICIAL LIQUIDATORS (DUTIES, POWERS AND FUNCTIONS)

Part-IV containing Sections 359 to 365 of the Companies Act, 2013 lays down the provisions relating to "Official Liquidators".

Meaning: Liquidation is a process by which the existence or life of a company is put to an end. To execute liquidation proceedings, a person is appointed to administer the assets and liabilities of the company. Such person or administrator is called 'Liquidator'. He is known as 'Official Liquidator' in case of compulsory winding up; and 'Liquidator' in case of voluntary winding up.

Company Liquidators and their appointment of Official Liquidators (Sec. 275): Section 275 of the Companies Act, 2013 (Corresponding to Section 448 of the Companies Act, 1956) provides for the appointment of official liquidators to take up the post winding up/liquidation process of a company. It runs as follows-

(*1*) For the purposes of winding up of a company by the Tribunal, the Tribunal at the time of the passing of the order of winding up, shall appoint an Official Liquidator or a liquidator from the panel maintained under sub-section (*2*) as the Company Liquidator.

(*2*) The provisional liquidator or the Company Liquidator, as the case may be, shall be appointed from a panel maintained by the Central Government consisting of the names of chartered accountants, advocates, company secretaries, cost accountants or firms or bodies corporate having such chartered accountants, advocates, company secretaries, cost accountants and such other professionals as may be notified by the Central Government or from a firm or a body corporate of persons having a combination of such professionals as may be prescribed and having at least ten years' experience in company matters.

(*3*) Where a provisional liquidator is appointed by the Tribunal, the Tribunal may limit and restrict his powers by the order appointing him or it or by a subsequent order, but otherwise he shall have the same powers as a liquidator.

(*4*) The Central Government may remove the name of any person or firm or body corporate from the panel maintained under sub-section (*2*) on the grounds of misconduct, fraud, misfeasance, breach of duties or professional incompetence:

Provided that the Central Government before removing him or it from the panel shall give him or it a reasonable opportunity of being heard.

(*5*) The terms and conditions of appointment of a provisional liquidator or Company Liquidator and the fee payable to him or it shall be specified by the Tribunal on the basis of task required to be performed, experience, qualification of such liquidator and size of the company.

(*6*) On appointment as provisional liquidator or Company Liquidator, as the case may be, such liquidator shall file a declaration within seven days from the date of appointment in the prescribed form disclosing conflict of interest or lack of independence in respect of his appointment, if any, with the Tribunal and such obligation shall continue throughout the term of his appointment.

(*7*) While passing a winding up order, the Tribunal may appoint a provisional liquidator, if any, appointed under clause (*c*) of sub-section (*1*) of section 273, as the Company Liquidator for the conduct of the proceedings for the winding up of the company.

The Supreme Court in ***M/s. Bakemans Industries (Pvt.) Ltd. v. M/s. New Kanpur Flour Mills Ltd. & Others (AIR 2008 SC 2699),*** held that a provisional liquidator appointed under Section 275 of the Companies Act, 2013 (Corresponding Section 451 of the Companies Act, 1956) shall all the powers and exercise all the functions which an official liquidator has been assigned under Section 290. But the Tribunal has the power to limit the powers and functions of the Provisional Liquidator, where it deems it necessary.

Official Liquidator to be Liquidator (Sec. 275): On a winding up order being made in respect of a company, the Official Liquidator shall, by virtue of the office, become the liquidator of the company.

Appointment and Powers of Provisional Liquidator (Sec.275): At any time after the presentation of a winding up petition and before making of a winding up order, the Tribunal may appoint the Official Liquidator to be the liquidator provisionally.

A provisional liquidator is as much a liquidator in winding up; in fact, the name provisional liquidator is only a convenient label ...he has the same powers and to the extent these powers imply duties, the same duties as a liquidator in a winding up. The Tribunal may limit and restrict his powers by the order appointing him or by a subsequent order. Otherwise, he has the same powers as a liquidator has.

Statement of Affairs to be made to Official Liquidator: Within 21 days of the date of the winding up order or of the appointment of the Official Liquidator as a provisional liquidator, the company has to submit to the Official Liquidator a statement as to the affairs of the company unless the Tribunal otherwise orders. The statement must contain the following particulars:

a) The assets of the company.

b) Its debts and liabilities.

c) The names, residences, and occupations of its creditors stating separately the amount of the secured and unsecured debts.

d) In the case of secured debts, the particulars of the securities given by the company or its officers.

e) The debts due to the company and the names, residences and occupations of the persons from whom they are due and the amount likely to be realised on account thereof.

f) Such further or other informations as may be prescribed or as the Official Liquidator may require.

The period of 21 days for the submission of the statement may be extended by the Tribunal to a maximum period of three months.

The statement is required to be verified by one or more of persons who are at the relevant date the directors and by the person who is at that date the manager, secretary or other Chief Officer of the company or by such of the persons as the Official Liquidator subject to the direction of the Tribunal, may require to submit and verify the statement.

The statement may be submitted and verified even by an ex-director of the company.

Report by Official Liquidator (Sec. 281): Section 281 of the Companies Act, 2013 (Corresponding to Section 455 of the Companies Act, 1956) envisages the submission of report by the Companies Liquidator. Section 281 provides that, in case, where winding up order is made, the Company Liquidator shall, as soon as practicable after receiving the Statement of Affairs, but not later than sixty days from the date of winding up order, submit a preliminary report to the Tribunal showing:

1. a) the nature and details of the assets of the company including their location and value, stating separately the cash balance in hand and in bank, if any, and the negotiable securities, if any, held by the company.

   b) the amount of capital issued, subscribed and paid up;

   c) existing and contingent liabilities with details of creditors etc.

   d) the debts due to the company with details of persons from whom it is due and the amount likely to be realized on account thereof;

   e) guarantees, if any, extended by the company;

   f) list of contributories and dues, if any, payable by them with details;

   g) details of trade-marks and intellectual properties owned by the company;

   h) details of subsisting contracts, joint-ventures and collaborations, if any;

i) details of holding and subsidiary companies, if any;

j) details of legal cases filed against or by the company; and

k) any other information which the Tribunal may direct or the Company Liquidator may consider necessary to include;

2. The Company Liquidator shall include in his report any fraud if committed by any person in the formation or promotion of the company and officer concerned who are involved therein.

3. He shall also make a report on the viability of the company's business or steps that are necessary for maximizing the value of the assets of the company.

4. The Company Liquidator may also make further report or reports if thinks it necessary to do so.

5. Any creditor or contributory of the company shall be entitled to inspect the report of the Company Liquidator at all reasonable times and take copies thereof or extracts there from on payment of the prescribed fees.

Powers, Duties and Functions of the Liquidator (Sec.290 & 360): The powers of the Liquidator may be explained as follows:

1. With previous sanction of the Tribunal.

2. Without the sanction of the Tribunal, and

3. Powers, which he can exercise with the leave of the Tribunal in case of onerous contracts.

However, it is to be noted that the Tribunal may provide that the liquidator may exercise any of the powers requiring the sanction of the Tribunal without the sanction of the Tribunal but the exercise of those powers by the liquidator will nonetheless be subject to the control of the Tribunal (Section 290(3).

The Supreme Court in ***Industrial Financial Corporation v. Official Liquidator, High Court of Calcutta (AIR 1993 SC 1524)*** observed that in case of sale of assets of a company in liquidation by Tribunal under Section 457(1) (now Section 290(1) of the 2013 Act) the Tribunal should formulate some method,

procedure and terms of sale so as to avoid negotiating the terms and conditions by the Tribunal with the party.

In ***Divya Manufacturing Co. v. Union of India*** **(AIR 2000 SC (2nd Suppl.) 2346)**, the Supreme Court has made it clear that the court (now Tribunal) is custodian of the interest of the company and its creditors. Hence, it is the duty of the court (now Tribunal) to see that the price fetched at the auction is an adequate price, even though there is no suggestion of irregularity or fraud. Confirmation of the sale by a court (now Tribunal) at grossly inadequate price, whether or not, it is a consequence of any irregularity or fraud in the conduct of sale could be set aside on the ground that it was not just and proper exercise of judicial discretion.

In ***Union Bank of India v. Official Liquidator*** **(AIR 2000 SC 3642)**, the Supreme Court has held that before sanctioning the sale of the company's assets, the court (now Tribunal) is required to exercise judicial discretion to see that the properties are sold at a reasonable price. For deciding what would be reasonable price, valuation report of an expert is must. In addition, it is the duty of the Tribunal to disclose the said valuation report to the secured creditors and other interested persons including the offerers. Further, it is the duty of the court (now Tribunal) to apply its mind to the valuation report for verifying whether the report indicates reasonable market value of the property to be auctioned, even if objections are not raised.

1. With previous sanction of the Tribunal: Liquidator is empowered –

i. To institute legal proceedings, civil and criminal, on behalf of the company.

ii. To carry on business if necessary for beneficial winding up.

iii. To sell or dispose of properties of the company both movable and immovable, by public auction or by private contracts.

iv. To raise loans on the security of the company's assets.

v. To do all other things as may be necessary.

The Supreme Court in ***Allahabad Bank v. Bengal Paper Mills Co. Ltd. & Others (AIR 1999 SC 1715)*** set aside the sale of assets and properties of winding up company on the ground that valuation of properties was suspicious and the publicity of sale was also not adequate. The Court observed that the sale had not procured the best possible price because it was conducted in undue haste. The mere fact that purchaser was allowed to take possession of properties on very next day of sale is not a ground for not setting aside the sale specially when appeals against sale were filed within limitation. Further, the fact of re-employment of 1700 workers of the company by the purchaser could not over weigh the interests of unsecured creditors.

In Allahabad V. ARC Holding Ltd. & Others (AIR 2000 SC 3098) was called upon to decide whether after an order passed in execution proceedings for the sale of plant, machinery and movable lying at the factory, can the same Court (now Tribunal) later pass an order for sale of the factory of the company as a 'going concern' setting aside its earlier order of execution of sale proceedings.

In ***D.C.M. Financial Services Ltd. v. Neel Kamal Plastics Ltd. (AIR 2002 SC 850)*** the Official Liquidator of the company which was in liquidation wanted to avail the benefit of the Non-performing Assets Scheme notified by the Reserve Bank of India for the disposal of part of property of the company. The said scheme if averted was giving company a substantial financial benefit which in turn could be made available for distribution amongst various creditors of the company. The Madras High Court had granted the permission the validity of which was challenged before the Supreme Court through a special leave petition.

2. Without the sanction of the court:

i. To execute all deeds in his name, on behalf of the company.

ii. He can inspect files and records of the company with the Registrar (of companies) without fee.

iii. To prove and claim the insolvency of any contributory for the balance due.

iv. To draw, accept and endorse any negotiable instrument on behalf of the company.

v. He can appoint an agent to attend his work.

vi. He may apply to the court for direction in any matter.

The exercise of the above powers is subject to the overall control of the Tribunal and any creditor or contributory may apply to the Tribunal with respect to the exercise of any power. The liquidator may also seek directions from the Tribunal in relation to any particular matter arising in the winding up. He can also call general meetings of the creditors and contributories and when one-tenth of the value of the creditors and contributories by resolution request him to do so, he is bound to hold such meetings.

In ***Ravindra Ishwardas Sethna v. Official Liquidator, High Court of Bombay (AIR 1983 SC 1001)*** the Supreme Court held that when a company is being wound up and the Company Liquidator takes over tenanted premises, then if the liquidator does not require the premises for carrying on the business of the company under Section 457 of the Companies Act, 1956 (now Section 292 of the Act 2013) or for the beneficial winding up of the company, the possession of the premises must be handed over to the landlord.

Power exercisable with the leave of the Tribunal in case of onerous contracts: There may be certain assets of the company which may be worthless or an unnecessary burden on the company and the creditors and contributories far from being interested in such assets, may prefer to do away with them. For example, shares which are not fully paid, onerous covenants, unprofitable contracts or short-term leases may be a liability rather than the asset and the Company Liquidator may like to get rid of them. This is called disclaimer and it operates in the interests of creditors and contributories by disposing on such unwanted assets of the company in liquidation. The liquidator may, with the leave of the Tribunal, disclaim in writing. The right of disclaimer has to be exercised by the Company Liquidator within twelve months after the commencement of the winding up.

The effect of disclaimer is to terminate the rights, interests and liabilities of the company in respect of the property which is disclaimed, but it does not affect the rights or liabilities of any other person except so far as is necessary to release the company from liability. However, the right of disclaimer is subject to following two conditions, namely:

i. Where any interested person in writing calls upon the Company Liquidator to decide whether or not he (i.e. liquidator) will disclaim, the power of disclaimer will be lost if the liquidator does not, within twenty eight days after receiving the application, give notice of his intention to apply to the Tribunal for leave to disclaim.

ii. If in case of a contract, the power to disclaim is lost as stated above, the company is deemed to have adopted the contract.

The disclaimer does not vest the property disclaimed in any person. But where a person claiming an interest in the disclaimed property, or under a liability in respect of it, applies to the Tribunal, the Tribunal may make an order vesting the property in any person entitled to it.

Any person aggrieved by the disclaimer is deemed to be a creditor of the company and may claim compensation amount as a debt in the winding up proceeding against the comp;any.

Control of the liquidators Powers: The liquidator is required to take into account the directions given to him by the resolutions of the creditors or contributory or by the committee of inspection.

He is to exercise his powers and functions under the supervision and control of the Tribunal.

Any person aggrieved by any act or decision of the liquidator may apply to the Tribunal and the Tribunal may confirm, reverse or modify the act or decision complained of and makes such further orders as it thinks just in the circumstances.

Duties of the Company Liquidator (Sec. 290): Following are the duties of the Liquidator.

1. Duty to take the property of the company in to his custody.
2. Duty to Settle List of Contributories.
3. Duty to admit or reject proof of debts.
4. Duty to make calls.
5. Duty to pay Company's debts.
6. Duty to keep Books, Papers, Documents, etc.
7. Duty to Report as to the progress of Liquidation.
8. Duty to Maintain proper accounts.
9. Duty to Distribute the Balance to Contributories.

1. Duty to take the property of the company in to his custody: Soon after his appointment, a liquidator or a provisional liquidator is required to take in to his custody and control all the property, effects and actionable claims of the company in liquidation. The property, effects and actionable claims, which the Liquidator takes into his possession, shall be deemed to be in custody of the Tribunal from the date of the winding up order.

The Tribunal may, at any time after making a winding up order, require any contributory, trustee, receiver, banker, agent or employee or officer of the company to deliver to the liquidator any money, property, books, documents or papers which are in his custody or control to which the company is prima facie entitled.

The liquidator is under a duty to set aside certain transactions such as a floating charge, transfer of property or delivery of goods or payments etc. in order to recover the property for the benefit of unsecured creditors. He can also recover any unauthorised profits made by directors by virtue of their position.

Liquidator should remit all moneys representing unclaimed or undistributed assets, which have remained in his hands for 6 months, into the public account of India in the Reserve Bank under a separate account called the 'Company's Liquidation Account'. Any such moneys remaining in his hands on the dissolution of the company must also be similarly remitted in to this account.

2. Duty to Settle List of Contributories: Section 285 of the Companies Act, 2013 (Contrry to Section 467 of the Companies Act, 1956) imposes a duty on the Official Liquidator to settle the list of contributories and rectify the register of members where required subject to the leave of the Tribunal. However, he cannot rectify the register of members without special leave of the Tribunal.

The Court may dispense with the settlement of the list of contributories where it appears that it will not be necessary to make calls or adjust the rights of contributories.

3. Duty to admit or reject proof of debts: The Law requires that all the creditors must formally prove the debts owed to them by the company by means of affidavits known as 'Proofs' unless the Tribunal orders the admission of debts of any creditor without such proof. A claim of debt which is barred by limitation at the commencement of the winding up cannot be lodged. So also a debt which is founded on an illegal or immoral consideration cannot be claimed.

The liquidator may admit or reject any proof of debt in whole or in part but every rejection must contain the grounds in writing. The creditor aggrieved by such rejection may file an appeal to the Tribunal within twenty-one days from the service of the notice of rejection.

4. Duty to make calls: Section 296 of the Companies Act, 2013 (Corresponding to Section 470 of the Companies Act, 1956) provides that the Tribunal is empowered to make calls on persons who are on the list of contributories in order to enforce their liability but this duty is delegated by the Tribunal to the Official Liquidator who is an officer of the Tribunal. The liquidator can make calls to the extent of amount necessary to satisfy the debts and liabilities of the company, and costs, charges and expenses needed for completion of the winding up process and to adjust the claims of the contributories among themselves. He can make an application supported by an affidavit, to the Tribunal for an order against any contributory for payment of money due on calls. Where the contributory attempts to abscond or dispose off property in order

to evade calls, he may be arrested and his property may be seized by the Tribunal.

Section 295(2) provides that contributory who is also a creditor of the company is not entitled to set off his debt against his liability for calls. However, after all the creditors have been paid in full, any debt due from the company to the contributory may be set off against calls.

5. Duty to pay Company's debts: The liquidator is under a duty to pay off the debts in full where the company is solvent and the assets of the company must not be distributed among the contributories unless the company's debt is fully paid. However, where the company is insolvent, the rules for payment to the secured and unsecured creditors as contained in the law of insolvency shall be applicable. It is only after the meeting, the costs of the winding up and paying off ordinary debts of secured creditors in full that the liquidator should pay the deferred debts, namely, the money owed to members in their capacity as members by way of dividend, profit, etc.

Section 298 of the Companies Act, 2013 provides that where the assets of the company in liquidation are insufficient to satisfy the liabilities, the Court may make an order for payment out of the assets of the costs, charges and expenses incurred in winding up in order of priority as it thinks just and reasonable.

6. Duty to keep Books, Papers, Documents, etc.: The liquidator is expected to maintain a number of registers and books and enter therein the minutes of proceedings of the meeting held from time to time. Any creditor or contributory can inspect such books and records on payment of prescribed fees but he is not entitled to inspect the account books.

7. Duty to Report as to the progress of Liquidation (Sec.248): Where the winding up of a company could not be concluded within one year, the liquidator is under a duty to file a statement in prescribed form within two months of the expiry of such year and thereafter at an interval of not more than one year, until the winding up is completed, with the winding up Tribunal. The

statement must be audited by a qualified auditor of the company. A Company of the statement should simultaneously be also filed with the Registrar of Companies and to the Central Government, if the company under liquidation is a government company. A creditor or contributory of the company; may inspect the statement and receive a copy or extract thereof, on payment of the prescribed fees.

Where the statement referred to above relates to a Government Company in liquidation, the Company Liquidator shall forward a copy of such statement –

a. To the Central Government, if the Government is a member of the Government company.

b. To the State Government, if the State Government is a member of the company.

c. To the Central Government and any State Government; if both the Governments are members of the Government Company.

If the Company Liquidator contravenes the provisions of Section 348 of the Act, 2013, he shall be punishable with fine which may extend to five thousand rupees for every day during which the default continues.

8. Duty to Maintain proper accounts: A liquidator has also to submit to the Tribunal twice a year, an account of his receipts and payments as liquidator. The accounts must be presented in the prescribed form and in duplicate and must be duly verified by the liquidator. The liquidator has to send a copy of the printed accounts to every creditor and contributory. A copy thereof is also to be filed with the Registrar of Companies.

The Tribunal shall cause the account to be audited and for this purpose it may require the liquidator to furnish such vouchers, information, registers, books etc. at the time of such audit.

9. Duty to Distribute the Balance to Contributors: When the liability of company to its creditors has been fully discharged, the liquidator should apply to the Court for leave to distribute surplus assets among the contributories. The distribution of surplus among the entitled contributories shall only be made when it has been duly

ordered by the Tribunal. The preference shareholders obviously will have preferential right over the equity shareholders in repayment of the capital paid up by them. The liquidator should take into consideration the provisions of the memorandum and articles of the company while distributing the surplus assets.

Advisory Committee (Sec.287): Section 287 of the Companies Act, 2013 provides that the Tribunal may order the appointment of Advisory Committee during the winding up proceeding of a company to advise the liquidator.

In case of compulsory winding up, the Tribunal may, at the time of making an order for winding up of the company or at any time thereafter, direct that a Committee of Inspection be appointed to act with the liquidator. The liquidator shall convene a meeting of the creditor within two months of the order of the Tribunal to nominate members to the Committee of Inspection. Within fourteen days of the Creditor's meeting, he shall also call a meeting of the contributories to consider the creditor's decision with respect to membership of the Committee. In case of any difference of opinion, the Liquidator shall apply to the Tribunal for directions as to the composition of the Committee of Inspection.

Section 287(2) of the Companies Act, 2013 provides that the Advisory Committee shall consist of not more than twelve members. It shall have the right to inspect the accounts of the liquidator. The quorum for a meeting of the Committee shall be one-third of its total membership or two, whichever is higher. The Committee shall act by majority decision. A member may resign by notice in writing delivered to the liquidator. A member, who is adjudged insolvent or absents himself from five consecutive meetings of the Committee without leave of absence or compounds with his creditors, shall cease to be a member and his office shall become vacant. The vacancy so caused may be filed by creditors or contributories, as the case may be.

The meetings of the Advisory Committee shall be chaired by the liquidator.

Lecture-XXII

COMPANIES INCORPORATED OUTSIDE INDIA (Sections 379 to 393)

Application of Act to foreign companies (Sec.379): [(1) Sections 380 to 386 (both inclusive) and sections 392 and 393 shall apply to all foreign companies:

Provided that the Central Government may, by Order published in the Official Gazette, exempt any class of foreign companies, specified in the Order, from any of the provisions of sections 380 to 386 and sections 392 and 393 and a copy of every such Order shall, as soon as may be after it is made, be laid before both Houses of Parliament.]

[(2)]Where not less than fifty per cent. of the paid-up share capital, whether equity or preference or partly equity and partly preference, of a foreign company is held by one or more citizens of India or by one or more companies or bodies corporate incorporated in India, or by one or more Citizens of India and one or more companies or bodies corporate incorporated in India, whether singly or in the aggregate, such company shall comply with the provisions of this Chapter and such other provisions of this Act as may be prescribed with regard to the business carried on by it in India as if it were a company incorporated in India.

Documents, etc. to be delivered to Registrar by foreign companies (Sec.380): (1) Every foreign company shall, within thirty days of the establishment of its place of business in India, deliver to the Registrar for registration:

(*a*) a certified copy of the charter, statutes or memorandum and articles, of the company or other instrument constituting or defining the constitution of the company and, if the instrument is not in the English language, a certified translation thereof in the English language;

(*b*) the full address of the registered or principal office of the company;

(*c*) a list of the directors and secretary of the company containing such particulars as may be prescribed;

(*d*) the name and address or the names and addresses of one or more persons resident in India authorised to accept on behalf of the company service of process and any notices or other documents required to be served on the company;

(e) the full address of the office of the company in India which is deemed to be its principal place of business in India;

(f) particulars of opening and closing of a place of business in India on earlier occasion or occasions;

(g) declaration that none of the directors of the company or the authorised representative in India has ever been convicted or debarred from formation of companies and management in India or abroad; and

(h) any other information as may be prescribed.

(*2*) Every foreign company existing at the commencement of this Act shall, if it has not delivered to the Registrar before such commencement, the documents and particulars specified in sub-section (*1*) of section 592 of the Companies Act, 1956 (1 of 1956), continue to be subject to the obligation to deliver those documents and particulars in accordance with that Act.

(3) Where any alteration is made or occurs in the documents delivered to the Registrar under this section, the foreign company shall, within thirty days of such alteration, deliver to the Registrar for registration, a return containing the particulars of the alteration in the prescribed form.

Accounts of foreign company (Sec.381): (1) Every foreign company shall, in every calendar year:

(a) make out a balance sheet and profit and loss account in such form, containing such particulars and including or having annexed or attached thereto such documents as may be prescribed; and

(b) deliver a copy of those documents to the Registrar:

Provided that the Central Government may, by notification, direct that, in the case of any foreign company or class of foreign companies, the requirements of clause (a) shall not apply, or shall apply subject to such exceptions and modifications as may be specified in that notification.

(2) If any such document as is mentioned in sub-section (1) is not in the English language, there shall be annexed to it a certified translation thereof in the English language.

(3) Every foreign company shall send to the Registrar along with the documents required to be delivered to him under sub-section (1), a copy of a list in the prescribed form of all places of business established by the company in India as at the date with reference to which the balance sheet referred to in sub-section (1) is made out.

Display of name, etc. of foreign company (Sec.382): Every foreign company shall:

(a) conspicuously exhibit on the outside of every office or place where it carries on business in India, the name of the company and the country in which it is incorporated, in letters easily legible in English characters, and also in the characters of the language or one of the languages in general use in the locality in which the office or place is situate;

(b) cause the name of the company and of the country in which the company is incorporated, to be stated in legible English characters in all business letters, billheads and letter paper, and in all notices, and other official publications of the company; and

(c) if the liability of the members of the company is limited, cause notice of that fact:

  (i) to be stated in every such prospectus issued and in all business letters, bill-heads, letter paper, notices, advertisements and other official publications of the company, in legible English characters; and

  (ii) to be conspicuously exhibited on the outside of every office or place where it carries on business in India, in legible English characters and also in legible characters of the language or one of the languages in general use in the locality in which the office or place is situate.

Service on foreign company (Sec.383): Any process, notice, or other document required to be served on a foreign company shall be deemed to be sufficiently served, if addressed to any person whose name and address have been delivered to the Registrar under

section 380 and left at, or sent by post to, the address which has been so delivered to the Registrar or by electronic mode.

Debentures, annual return, registration of charges, books of account and their inspection (Sec.384): (1) The provisions of Section 71 shall apply *mutatis mutandis* to a foreign company.

(2) The provisions of Section 92 [and section 135] shall, subject to such exceptions, modifications and adaptations as may be made therein by rules made under this Act, apply to a foreign company as they apply to a company incorporated in India.

(3) The provisions of Section 128 shall apply to a foreign company to the extent of requiring it to keep at its principal place of business in India, the books of account referred to in that section, with respect to monies received and spent, sales and purchases made, and assets and liabilities, in the course of or in relation to its business in India.

(4) The provisions of Chapter VI shall apply *mutatis mutandis* to charges on properties which are created or acquired by any foreign company.

(5) The provisions of Chapter XIV shall apply *mutatis mutandis* to the Indian business of a foreign company as they apply to a company incorporated in India.

Fee for registration of documents (Sec.385): There shall be paid to the Registrar for registering any document required by the provisions of this Chapter to be registered by him, such fee, as may be prescribed.

Interpretation (Sec.386): For the purposes of the foregoing provisions of this Chapter:

(a) the expression "certified" means certified in the prescribed manner to be a true copy or a correct translation;

(b) the expression "director", in relation to a foreign company, includes any person in accordance with whose directions or instructions the Board of Directors of the company is accustomed to act; and

(c) the expression "place of business" includes a share transfer or registration office.

Dating of prospectus and particulars to be contained therein (Sec.387): (1) No person shall issue, circulate or distribute in India any prospectus offering to subscribe for securities of a company incorporated or to be incorporated outside India, whether the company has or has not established, or when formed will or will not establish, a place of business in India, unless the prospectus is dated and signed, and:

(a) contains particulars with respect to the following matters, namely:

(i) the instrument constituting or defining the constitution of the company;

(ii) the enactments or provisions by or under which the incorporation of the company was effected;

(iii) address in India where the said instrument, enactments or provisions, or copies thereof, and if the same are not in the English language, a certified translation thereof in the English language can be inspected;

(iv) the date on which and the country in which the company would be or was incorporated; and

(v) whether the company has established a place of business in India and, if so, the address of its principal office in India; and

(b) states the matters specified under section 26:

Provided that sub-clauses (i), (ii) and (iii) of clause (a) of this sub-section shall not apply in the case of a prospectus issued more than two years after the date at which the company is entitled to commence business.

(2) Any condition requiring or binding an applicant for securities to waive compliance with any requirement imposed by virtue of sub-section (1), or purporting to impute him with notice of any contract, documents or matter not specifically referred to in the prospectus, shall be void.

(3) No person shall issue to any person in India a form of application for securities of such a company or intended company as is mentioned in sub-section (1), unless the form is issued with a prospectus which complies with the provisions of this Chapter and such issue does not contravene the provisions of section 388:

Provided that this sub-section shall not apply if it is shown that the form of application was issued in connection with a *bona fide* invitation to a person to enter into an underwriting agreement with respect to securities.

(4) This section:

(a) shall not apply to the issue to existing members or debenture holders of a company of a prospectus or form of application relating to securities of the company, whether an applicant for securities will or will not have the right to renounce in favour of other persons; and

(b) except in so far as it requires a prospectus to be dated, to the issue of a prospectus relating to securities which are or are to be in all respects uniform with securities previously issued and for the time being dealt in or quoted on a recognised stock exchange,

but, subject as aforesaid, this section shall apply to a prospectus or form of application whether issued on or with reference to the formation of a company or subsequently.

(5) Nothing in this section shall limit or diminish any liability which any person may incur under any law for the time being in force in India or under this Act apart from this section.

Provisions as to expert's consent and allotment (Sec.388): (1) No person shall issue, circulate or distribute in India any prospectus offering for subscription in securities of a company incorporated or to be incorporated outside India, whether the company has or has not been established, or when formed will or will not establish, a place of business in India:

(a) if, where the prospectus includes a statement purporting to be made by an expert, he has not given, or has before delivery of the prospectus for registration withdrawn, his written consent to the issue of the prospectus with the statement included in the form and context in which it is included, or there does not appear in the prospectus a statement that he has given and has not withdrawn his consent as aforesaid; or

(b) if the prospectus does not have the effect, where an application is made in pursuance thereof, of rendering all persons concerned bound by all the provisions of Sections 33 and 40, so far as applicable.

(2) For the purposes of this section, a statement shall be deemed to be included in a prospectus, if it is contained in any report or memorandum appearing on the face thereof or by reference incorporated therein or issued therewith.

Registration of prospectus (Sec.389): No person shall issue, circulate or distribute in India any prospectus offering for subscription in securities of a company incorporated or to be incorporated outside India, whether the company has or has not established, or when formed will or will not establish, a place of business in India, unless before the issue, circulation or distribution of the prospectus in India, a copy thereof certified by the chairperson of the company and two other directors of the company as having been approved by resolution of the managing body has been delivered for registration to the Registrar and the prospectus states on the face of it that a copy has been so delivered, and there is endorsed on or attached to the copy, any consent to the issue of the prospectus required by section 388 and such documents as may be prescribed.

Offer of Indian Depository Receipts (Sec.390): Notwithstanding anything contained in any other law for the time being in force, the Central Government may make rules applicable for:

(*a*) the offer of Indian Depository Receipts;

(*b*) the requirement of disclosures in prospectus or letter of offer issued in connection with Indian Depository Receipts;

(*c*) the manner in which the Indian Depository Receipts shall be dealt with in a depository mode and by custodian and underwriters; and

(*d*) the manner of sale, transfer or transmission of Indian Depository Receipts,

by a company incorporated or to be incorporated outside India, whether the company has or has not established, or will or will not establish, any place of business in India.

Application of Sections 34 to 36 and Chapter XX (Sec.391): (1) The provisions of sections 34 to 36 (both inclusive) shall apply to:

(i) the issue of a prospectus by a company incorporated outside India under Section 389 as they apply to prospectus issued by an Indian company;

(ii) the issue of Indian Depository Receipts by a foreign company.

[(2) Subject to the provisions of section 376, the provisions of Chapter XX shall apply mutatis mutandis for closure of the place of business of a foreign company in India as if it were a company incorporated in India in case such foreign company has raised monies through offer or issue of securities under this Chapter which have not been repaid or redeemed.]

Punishment for contravention (Sec.392): Without prejudice to the provisions of section 391, if a foreign company contravenes the provisions of this Chapter, the foreign company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to three lakh rupees and in the case of a continuing offence, with an additional fine which may extend to fifty thousand rupees for every day after the first during which the contravention continues and every officer of the foreign company who is in default shall be punishable with imprisonment for a term which may extend

to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees, or with both.

Company's failure to comply with provisions of this Chapter not to affect validity of contracts, etc. (Sec.393): Any failure by a company to comply with the provisions of this Chapter shall not affect the validity of any contract, dealing or transaction entered into by the company or its liability to be sued in respect thereof, but the company shall not be entitled to bring any suit, claim any set-off, make any counter-claim or institute any legal proceeding in respect of any such contract, dealing or transaction, until the company has complied with the provisions of this Act applicable to it.

Lecture – XXIII

GOVERNMENT COMPANIES (Sections 394 and 395)

Annual reports on Government Companies (Sec.394): (1) Where the Central Government is a member of a Government company, the Central Government shall cause an annual report on the working and affairs of that company to be:

(a) prepared within three months of its annual general meeting before which the comments given by the Comptroller and Auditor-General of India and the audit report is placed under the proviso to sub-section (*6*) of section 143; and

(b) as soon as may be after such preparation, laid before both Houses of Parliament together with a copy of the audit report and comments upon or supplement to the audit report, made by the Comptroller and Auditor-General of India.

(*2*) Where in addition to the Central Government, any State Government is also a member of a Government company, that State Government shall cause a copy of the annual report prepared under sub-section (*1*) to be laid before the House or both Houses of the State Legislature together with a copy of the audit report and the comments upon or supplement to the audit report referred to in sub-section (1).

Annual reports where one or more State Governments are members of companies (Sec.395): (1) Where the Central Government is not a member of a Government company, every State Government which is a member of that company, or where only one State Government is a member of the company, that State Government shall cause an annual report on the working and affairs of the company to be:

(a) prepared within the time specified in sub-section (*1*) of section 394; and

(b) as soon as may be after such preparation, laid before the House or both Houses of the State Legislature together with a copy

of the audit report and comments upon or supplement to the audit report referred to in sub-section (*1*) of that section.

(*2*) The provisions of this section and section 394 shall, so far as may be, apply to a Government company in liquidation as they apply to any other Government company.

Lecture-XXIV

NIDHIS (Section 406)

Provision relating to *Nidhi's* and its application, etc. (Sec. 406): (1) In this section, *"Nidhi"* or *"Mutual Benefit Society"* means a company which the Central Government may, by notification in the Official Gazette, declare to be a Nidhi or Mutual Benefit Society, as the case may be.

(2) The Central Government may, by notification in the Official Gazette, direct that any of the provisions of this Act specified in the notification:

(a) shall not apply to any Nidhi or Mutual Benefit Society; or

(b) shall apply to any Nidhi or Mutual Benefit Society with such exceptions, modifications and adaptations as may be specified in the notification.

(3) A copy of every notification proposed to be issued under sub-section (2), shall be laid in draft before each House of Parliament, while it is in session, for a total period of thirty days, and if, both Houses agree in disapproving the issue of notification or both Houses agree in making any modification in the notification, the notification shall not be issued or, as the case may be, shall be issued only in such modified form as may be agreed upon by both the Houses.

(4) In reckoning any such period of thirty days as is referred to in sub-section (3), no account shall be taken of any period during which the House referred to in sub-section (3) is prorogued or adjourned for more than four consecutive days.

(5) The copies of every notification issued under this section shall, as soon as may be after it has been issued, be laid before each House of Parliament.

Lecture – XXV

NATIONAL COMPANY LAW TRIBUNAL (NCLT) AND APPELLATE TRIBUNAL (NCLAT)

Definition of 'Chairperson', 'Judicial Member', 'Member', 'President' and 'Technical Member' of the Tribunal (Sec.407): In this Chapter, unless the context otherwise requires:

(*a*) *"Chairperson"* means the Chairperson of the Appellate Tribunal;

(*b*) *"Judicial Member"* means a member of the Tribunal or the Appellate Tribunal appointed as such and includes the President or the Chairperson, as the case may be;

(*c*) *"Member"* means a member, whether Judicial or Technical of the Tribunal or the Appellate Tribunal and includes the President or the Chairperson, as the case may be;

(*d*) *"President"* means the President of the Tribunal;

(*e*) *"Technical Member"* means a member of the Tribunal or the Appellate Tribunal appointed as such.

Constitution of National Company Law Tribunal (NCLT) (Sec.408): The Central Government shall, by notification, constitute, with effect from such date as may be specified therein, a Tribunal to be known as the National Company Law Tribunal consisting of a President and such number of Judicial and Technical members, as the Central Government may deem necessary, to be appointed by it by notification, to exercise and discharge such powers and functions as are, or may be, conferred on it by or under this Act or any other law for the time being in force.

Constitution of NCLT: S.O. 1932(E), dt. 1-6-2016: In exercise of the powers conferred by section 408 of the Companies Act, 2013 (18 of 2013), the Central Government hereby constitutes the National Company Law Tribunal to exercise and discharge the powers and functions as are, or may be, conferred on it by or under the said Act with effect from the 1st day of June, 2016.

Qualification of President and Members of Tribunal (Sec.409): (*1*) The President shall be a person who is or has been a Judge of a High Court for five years.

(*2*) A person shall not be qualified for appointment as a Judicial Member unless he:

(*a*) is, or has been, a judge of a High Court; or

(*b*) is, or has been, a District Judge for at least five years; or

(*c*) has, for at least ten years been an advocate of a court.

Explanation: For the purposes of clause (*c*), in computing the period during which a person has been an advocate of a court, there shall be included any period during which the person has held judicial office or the office of a member of a tribunal or any post, under the Union or a State, requiring special knowledge of law after he become an advocate.

(*3*) A person shall not be qualified for appointment as a Technical Member unless he:

(*a*) has, for at least fifteen years been a member of the Indian Corporate Law Service or Indian Legal Service [and has been holding the rank of Secretary or Additional Secretary to the Government of India]; or

(*b*) is, or has been, in practice as a chartered accountant for at least fifteen years; or

(*c*) is, or has been, in practice as a cost accountant for at least fifteen years; or

(*d*) is, or has been, in practice as a company secretary for at least fifteen years; or

[(*e*) is a person of proven ability, integrity and standing having special knowledge and professional experience of not less than fifteen years in industrial finance, industrial management, industrial reconstruction, investment and accountancy.] or

(*f*) is, or has been, for at least five years, a presiding officer of a Labour Court, Tribunal or National Tribunal constituted under the Industrial Disputes Act, 1947 (14 of 1947).

Constitution of Appellate Tribunal (NCLAT) (Sec.410): The Central Government shall, by notification, constitute, with effect from such date as may be specified therein, an Appellate Tribunal to be known as the National Company Law Appellate Tribunal consisting of a chairperson and such number of Judicial and Technical Members, not exceeding eleven, as the Central Government may

deem fit, to be appointed by it by notification, for hearing appeals against

(a) the orders of the Tribunal or of the National Financial Reporting Authority under this Act, and

(b) any direction, decision or order referred to in S.53N of the Competition Act, 2002 in accordance with the provisions of that Act.

Constitution of NCLAT: S.O. 1933(E), dt. 1-6-2016: In exercise of the powers conferred by section 410 of the Companies Act, 2013 (18 of 2013), the Central Government hereby constitutes the National Company Law Appellate Tribunal for hearing appeals against the orders of the National Company Law Tribunal with effect from the 1st day of June, 2016.

Qualifications of Chairperson and Members of Appellate Tribunal (Sec.411): (1) The Chairperson shall be a person who is or has been a Judge of the Supreme Court or the Chief Justice of a High Court.

(2) A Judicial Member shall be a person who is or has been a Judge of a High Court or is a Judicial Member of the Tribunal for five years.

(3) A technical member shall be a person of proven ability, integrity and standing having special knowledge and professional experience of not less than twenty-five years in industrial finance, industrial management, industrial reconstruction, investment and accountancy.

Selection of Members of Tribunal and Appellate Tribunal (Sec.412): (1) The President of the Tribunal and the Chairperson and Judicial Members of the Appellate Tribunal, shall be appointed after consultation with the Chief Justice of India.

(2) The Members of the Tribunal and the Technical Members of the Appellate Tribunal shall be appointed on the recommendation of a Selection Committee consisting of—

(a) Chief Justice of India or his nominee—Chairperson;

(b) a senior Judge of the Supreme Court or Chief Justice of High Court— Member;

(c) Secretary in the Ministry of Corporate Affairs—Member; and

(d) Secretary in the Ministry of Law and Justice—Member.

(2A) Where in a meeting of the Selection Committee, there is equality of votes on any matter, the Chairperson shall have a casting vote.

(3) The Secretary, Ministry of Corporate Affairs shall be the Convener of the Selection Committee.

(*4*) The Selection Committee shall determine its procedure for recommending persons under sub-section (*2*).

(*5*) No appointment of the Members of the Tribunal or the Appellate Tribunal shall be invalid merely by reason of any vacancy or any defect in the constitution of the Selection Committee.

Term of office of President, Chairperson and other Members (Sec.413): (*1*) The President and every other Member of the Tribunal shall hold office as such for a term of five years from the date on which he enters upon his office, but shall be eligible for re-appointment for another term of five years.

(*2*) A Member of the Tribunal shall hold office as such until he attains,—

(*a*) in the case of the President, the age of sixty-seven years;

(*b*) in the case of any other Member, the age of sixty-five years:

Provided that a person who has not completed fifty years of age shall not be eligible for appointment as Member:

Provided further that the Member may retain his lien with his parent cadre or Ministry or Department, as the case may be, while holding office as such for a period not exceeding one year.

(*3*) The Chairperson or a Member of the Appellate Tribunal shall hold office as such for a term of five years from the date on which he enters upon his office, but shall be eligible for re-appointment for another term of five years.

(*4*) A Member of the Appellate Tribunal shall hold office as such until he attains:

(*a*) in the case of the Chairperson, the age of seventy years;

(*b*) in the case of any other Member, the age of sixty-seven years:

Provided that a person who has not completed fifty years of age shall not be eligible for appointment as Member:

Provided further that the Member may retain his lien with his parent cadre or Ministry or Department, as the case may be, while holding office as such for a period not exceeding one year.

Salary, allowances and other terms and conditions of service of Members (Sec.414): The salary, allowances and other terms and conditions of service of the Members of the Tribunal and the Appellate Tribunal shall be such as may be prescribed:

Provided that neither the salary and allowances nor the other terms and conditions of service of the Members shall be varied to their disadvantage after their appointment.

Acting President and Chairperson of Tribunal or Appellate Tribunal (Sec.415): (*1*) In the event of the occurrence of any vacancy in the office of the President or the Chairperson by reason of his death, resignation or otherwise, the senior-most Member shall act as the President or the Chairperson, as the case may be, until the date on which a new President or Chairperson appointed in accordance with the provisions of this Act to fill such vacancy enters upon his office.

(*2*) When the President or the Chairperson is unable to discharge his functions owing to absence, illness or any other cause, the senior-most Member shall discharge the functions of the President or the Chairperson, as the case may be, until the date on which the President or the Chairperson resumes his duties.

Resignation of Members (Sec.416): The President, the Chairperson or any Member may, by notice in writing under his hand addressed to the Central Government, resign from his office:

Provided that the President, the Chairperson, or the Member shall continue to hold office until the expiry of three months from the date of receipt of such notice by the Central Government or until a person duly appointed as his successor enters upon his office or until the expiry of his term of office, whichever is earliest..

Removal of Members (Sec.417): (1) The Central Government may, after consultation with the Chief Justice of India, remove from office the President, Chairperson or any Member, who:

(*a*) has been adjudged an insolvent; or

(*b*) has been convicted of an offence which, in the opinion of the Central Government, involves moral turpitude; or

(*c*) has become physically or mentally incapable of acting as such President, the Chairperson, or Member; or

(*d*) has acquired such financial or other interest as is likely to affect prejudicially his functions as such President, the Chairperson or Member; or

(*e*) has so abused his position as to render his continuance in office prejudicial to the public interest:

Provided that the President, the Chairperson or the Member shall not be removed on any of the grounds specified in clauses (*b*) to (*e*) without giving him a reasonable opportunity of being heard.

(*2*) Without prejudice to the provisions of sub-section (*1*), the President, the Chairperson or the Member shall not be removed from his office except by an order made by the Central Government on the ground of proved misbehaviour or incapacity after an inquiry made by a Judge of the Supreme Court nominated by the Chief Justice of India on a reference made to him by the Central Government in which such President, the Chairperson or Member had been informed of the charges against him and given a reasonable opportunity of being heard.

(*3*) The Central Government may, with the concurrence of the Chief Justice of India, suspend from office, the President, the Chairperson or Member in respect of whom reference has been made to the Judge of the Supreme Court under sub-section (*2*) until the Central Government has passed orders on receipt of the report of the Judge of the Supreme Court on such reference.

(*4*) The Central Government shall, after consultation with the Supreme Court, make rules to regulate the procedure for the inquiry on the ground of proved misbehaviour or incapacity referred to in sub-section (*2*).

[1][**417A.** Notwithstanding anything contained in this Act, the qualifications, appointment, term of office, salaries and allowances, resignation, removal and other terms and conditions of service of the Chairperson and other Members of the Appellate Tribunal appointed after the commencement of Part XIV of Chapter VI of the Finance Act, 2017, shall be governed by the provisions of Section 184 of that Act:

Provided that the Chairperson and Member appointed before the commencement of Part XIV of Chapter VI of the Finance Act, 2017, shall continue to be governed by the provisions of this Act and the rules made thereunder as if the provisions of Section 184 of the Finance Act, 2017 had not come into force.]

1. Ins. by Finance Act, 2017, w.e.f. 26-5-217, vide Noti. No. S.O. 1696(E), dt. 26-5-2017.

Staff of Tribunal and Appellate Tribunal (Sec.418): (*1*) The Central Government shall, in consultation with the Tribunal and the Appellate Tribunal, provide the Tribunal and the Appellate Tribunal, as the case may be, with such officers and other employees as may be necessary for the exercise of the powers and discharge of the functions of the Tribunal and the Appellate Tribunal.

(*2*) The officers and other employees of the Tribunal and the Appellate Tribunal shall discharge their functions under the general superintendence and control of the President, or as the case may be, the Chairperson, or any other Member to whom powers for exercising such superintendence and control are delegated by him.

(*3*) The salaries and allowances and other conditions of service of the officers and other employees of the Tribunal and the Appellate Tribunal shall be such as may be prescribed.

Benches of Tribunal (Sec.419): (*1*) There shall be constituted such number of Benches of the Tribunal, as may, by notification, be specified by the Central Government.

(*2*) The Principal Bench of the Tribunal shall be at New Delhi which shall be presided over by the President of the Tribunal.

(*3*) The powers of the Tribunal shall be exercisable by Benches consisting of two Members out of whom one shall be a Judicial Member and the other shall be a Technical Member:

Provided that it shall be competent for the Members of the Tribunal authorised in this behalf to function as a Bench consisting of a single Judicial Member and exercise the powers of the Tribunal in respect of such class of cases or such matters pertaining to such class of cases, as the President may, by general or special order, specify:

Provided further that if at any stage of the hearing of any such case or matter, it appears to the Member that the case or matter is of such a nature that it ought to be heard by a Bench consisting of two Members, the case or matter may be transferred by the President, or, as the case may be, referred to him for transfer, to such Bench as the President may deem fit.

(4) The Central Government shall, by notification, establish such number of benches of the Tribunal, as it may consider necessary, to exercise the jurisdiction, powers and authority of the Adjudicating Authority conferred on such Tribunal by or under Part II of the Insolvency and Bankruptcy Code, 2016.

(5) If the Members of a Bench differ in opinion on any point or points, it shall be decided according to the majority, if there is a majority, but if the Members are equally divided, they shall state the point or points on which they differ, and the case shall be referred by the President for hearing on such point or points by one or more of the other Members of the Tribunal and such point or points shall be decided according to the opinion of the majority of Members who have heard the case, including those who first heard it.

Orders of Tribunal (Sec.420): (*1*) The Tribunal may, after giving the parties to any proceeding before it, a reasonable opportunity of being heard, pass such orders thereon as it thinks fit.

(*2*) The Tribunal may, at any time within two years from the date of the order, with a view to rectifying any mistake apparent from the record, amend any order passed by it, and shall make such amendment, if the mistake is brought to its notice by the parties:

Provided that no such amendment shall be made in respect of any order against which an appeal has been preferred under this Act.

(*3*) The Tribunal shall send a copy of every order passed under this section to all the parties concerned.

Appeal from orders of Tribunal (NCLT) (Sec.421): *(1)* Any person aggrieved by an order of the Tribunal may prefer an appeal to the Appellate Tribunal.

(2) No appeal shall lie to the Appellate Tribunal from an order made by the Tribunal with the consent of parties.

(3) Every appeal under sub-section *(1)* shall be filed within a period of forty-five days from the date on which a copy of the order of the Tribunal is made available to the person aggrieved and shall be in such form, and accompanied by such fees, as may be prescribed:

Provided that the Appellate Tribunal may entertain an appeal after the expiry of the said period of forty-five days from the date aforesaid, but within a further period not exceeding forty-five days, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within that period.

(4) On the receipt of an appeal under sub-section *(1)*, the Appellate Tribunal shall, after giving the parties to the appeal a reasonable opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or setting aside the order appealed against.

(5) The Appellate Tribunal shall send a copy of every order made by it to the Tribunal and the parties to appeal.

Expeditious disposal by Tribunal and Appellate Tribunal (Sec.422): (*1*) Every application or petition presented before the Tribunal and every appeal filed before the Appellate Tribunal shall be dealt with and disposed of by it as expeditiously as possible and every endeavour shall be made by the Tribunal or the Appellate Tribunal, as the case may be, for the disposal of such application or petition or appeal within three months from the date of its presentation before the Tribunal or the filing of the appeal before the Appellate Tribunal.

(*2*) Where any application or petition or appeal is not disposed of within the period specified in sub-section (*1*), the Tribunal or, as the case may be, the Appellate Tribunal, shall record the reasons for not disposing of the application or petition or the appeal, as the case may be, within the period so specified; and the President or the Chairperson, as the case may be, may, after taking into account the reasons so recorded, extend the period referred to in sub-section (*1*) by such period not exceeding ninety days as he may consider necessary.

Appeal to Supreme Court (Sec.423): Any person aggrieved by any order of the Appellate Tribunal may file an appeal to the Supreme Court within sixty days from the date of receipt of the order of the Appellate Tribunal to him on any question of law arising out of such order:

Provided that the Supreme Court may, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal within the said period, allow it to be filed within a further period not exceeding sixty days.

Procedure before Tribunal and Appellate Tribunal (Sec.424): (*1*) The Tribunal and the Appellate Tribunal shall not, while disposing of any proceeding before it or, as the case may be, an appeal before it, be bound by the procedure laid down in the Code of Civil Procedure, 1908 (5 of 1908), but shall be guided by the principles of natural justice, and, subject to the other provisions of this Act or of the Insolvency and Bankruptcy Code, 2016 and of any rules made thereunder, the Tribunal and the Appellate Tribunal shall have power to regulate their own procedure.

(*2*) The Tribunal and the Appellate Tribunal shall have, for the purposes of discharging their functions under this Act, or under the Insolvency and Bankruptcy Code, 2016 the same powers as are vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908) while trying a suit in respect of the following matters, namely:

(*a*) summoning and enforcing the attendance of any person and examining him on oath;

(*b*) requiring the discovery and production of documents;

(*c*) receiving evidence on affidavits;

(*d*) subject to the provisions of sections 123 and 124 of the Indian Evidence Act, 1872 (1 of 1872), requisitioning any public record or document or a copy of such record or document from any office;

(*e*) issuing commissions for the examination of witnesses or documents;

(*f*) dismissing a representation for default or deciding it *ex parte;*

(*g*) setting aside any order of dismissal of any representation for default or any order passed by it *ex parte;* and

(*h*) any other matter which may be prescribed.

(*3*) Any order made by the Tribunal or the Appellate Tribunal may be enforced by that Tribunal in the same manner as if it were a decree made by a court in a suit pending therein, and it shall be lawful for the Tribunal or the Appellate Tribunal to send for execution of its orders to the court within the local limits of whose jurisdiction:

(*a*) in the case of an order against a company, the registered office of the company is situate; or

(*b*) in the case of an order against any other person, the person concerned voluntarily resides or carries on business or personally works for gain.

(*4*) All proceedings before the Tribunal or the Appellate Tribunal shall be deemed to be judicial proceedings within the meaning of sections 193 and 228, and for the purposes of section 196 of the Indian Penal Code (45 of 1860), and the Tribunal and the Appellate Tribunal shall be deemed to be civil court for the purposes of section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973 (2 of 1974).

Power to punish for contempt (Sec.425): The Tribunal and the Appellate Tribunal shall have the same jurisdiction, powers and authority in respect of contempt of themselves as the High Court has and may exercise, for this purpose, the powers under the provisions of the Contempt of Courts Act, 1971 (70 of 1971), which shall have the effect subject to modifications that:

(*a*) the reference therein to a High Court shall be construed as including a reference to the Tribunal and the Appellate Tribunal; and

(*b*) the reference to Advocate-General in section 15 of the said Act shall be construed as a reference to such Law Officers as the Central Government may, specify in this behalf.

Delegation of powers (Sec.426): The Tribunal or the Appellate Tribunal may, by general or special order, direct, subject to such conditions, if any, as may be specified in the order, any of its officers or employees or any other person authorised by it to inquire into any matter connected with any proceeding or, as the case may

be, appeal before it and to report to it in such manner as may be specified in the order.

President, Members, Officers, etc. to be public servants (Sec.427): The President, Members, officers and other employees of the Tribunal and the Chairperson, Members, officers and other employees of the Appellate Tribunal shall be deemed to be public servants within the meaning of section 21 of the Indian Penal Code (45 of 1860).

Protection of action taken in good faith (Sec.428): No suit, prosecution or other legal proceeding shall lie against the Tribunal, the President, Member, officer or other employee, or against the Appellate Tribunal, the Chairperson, Member, officer or other employees thereof or liquidator or any other person authorised by the Tribunal or the Appellate Tribunal for the discharge of any function under this Act in respect of any loss or damage caused or likely to be caused by any act which is in good faith done or intended to be done in pursuance of this Act.

Power to seek assistance of Chief Metropolitan Magistrate, etc. (Sec.429): (*1*) The Tribunal may, in any proceedings for winding up of a company under this Act or in any proceedings under the Insolvency and Bankruptcy Code, 2016, in order to take into custody or under its control all property, books of account or other documents, request, in writing, the Chief Metropolitan Magistrate, Chief Judicial Magistrate or the District Collector within whose jurisdiction any such property, books of account or other documents of such company under this Act or of corporate persons under the said Code, are situated or found, to take possession thereof, and the Chief Metropolitan Magistrate, Chief Judicial Magistrate or the District Collector, as the case may be, shall, on such request being made to him-

(a) take possession of such property, books of account or other documents; and

(b) cause the same to be entrusted to the Tribunal or other persons authorized by it.

(*2*) For the purpose of securing compliance with the provisions of sub-section (*1*), the Chief Metropolitan Magistrate, Chief Judicial Magistrate or the District Collector may take or cause to be taken such steps and use or cause to be used such force as may, in his opinion, be necessary.

(*3*) No act of the Chief Metropolitan Magistrate, Chief Judicial Magistrate or the District Collector done in pursuance of this section shall be called in question in any court or before any authority on any ground whatsoever.

Civil Court not to have jurisdiction (Sec.430): No Civil Court shall have jurisdiction to entertain any suit or proceeding in respect of any matter which the Tribunal or the Appellate Tribunal is empowered to determine by or under this Act or any other law for the time being in force and no injunction shall be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any power conferred by or under this Act or any other law for the time being in force, by the Tribunal or the Appellate Tribunal.

Vacancy in Tribunal or Appellate Tribunal not to invalidate acts or proceedings (Sec.431): No act or proceeding of the Tribunal or the Appellate Tribunal shall be questioned or shall be invalid merely on the ground of the existence of any vacancy or defect in the constitution of the Tribunal or the Appellate Tribunal, as the case may be.

Right to legal representation (Sec.432): A party to any proceeding or appeal before the Tribunal or the Appellate Tribunal, as the case may be, may either appear in person or authorise one or more chartered accountants or company secretaries or cost accountants or legal practitioners or any other person to present his case before the Tribunal or the Appellate Tribunal, as the case may be.

Limitation (Sec.433): The provisions of the Limitation Act, 1963 (36 of 1963) shall, as far as may be, apply to proceedings or appeals before the Tribunal or the Appellate Tribunal, as the case may be.

Transfer of certain pending proceedings (Sec.434): (1) On such date as may be notified by the Central Government in this behalf:

(a) all matters, proceedings or cases pending before the Board of Company Law Administration (herein in this section referred to as the Company Law Board) constituted under sub-section (1) of section 10E of the Companies Act, 1956 (1 of 1956), immediately before such date shall stand transferred to the Tribunal and the Tribunal shall dispose of such matters, proceedings or cases in accordance with the provisions of this Act;

(b) any person aggrieved by any decision or order of the Company Law Board made before such date may file an appeal to the High Court within sixty days from the date of communication of the decision or order of the Company Law Board to him on any question of law arising out of such order:

Provided that the High Court may if it is satisfied that the appellant was prevented by sufficient cause from filing an appeal within the said period, allow it to be filed within a further period not exceeding sixty days; and

(c) all proceedings under the Companies Act, 1956 (1 of 1956), including proceedings relating to arbitration, compromise, arrangements and reconstruction and winding up of companies, pending immediately before such date before any District Court or High Court, shall stand transferred to the Tribunal and the Tribunal may proceed to deal with such proceedings from the stage before their transfer:

Provided that only such proceedings relating to the winding up of companies shall be transferred to the Tribunal that are at a stage as may be prescribed by the Central Government:

Provided further that only such proceedings relating to cases other than winding-up, for which orders for allowing or otherwise of the proceedings are not reserved by the High Courts shall be transferred to the Tribunal:

Provided also that-

(i) all proceedings under the Companies Act, 1956 other than the cases relating to winding up of companies that are reserved for orders for allowing or otherwise such proceedings; or

(ii) the proceedings relating to winding up of companies which have not been transferred from the High Courts;

shall be dealt with in accordance with provisions of the Companies Act, 1956 and the Companies (Court) Rules, 1959.

Provided also that proceedings relating to cases of voluntary winding up of a company, where notice of the resolution by advertisement has been given under sub-section (1) of section 485 of the Companies Act, 1956 but the company has not been dissolved before the 1st April, 2017 shall continue to be dealt with in accordance with provisions of the Companies Act, 1956 and the Companies (Court) Rules, 1959:

Provided further that any party or parties to any proceedings relating to the winding up of companies pending before any Court immediately before the commencement of the Insolvency and Bankruptcy Code (Amendment) Ordinance, 2018, may file an application for transfer of such proceedings and the Court may by order transfer such proceedings to the Tribunal and the proceedings so transferred shall be dealt with by the Tribunal as an application for initiation of corporate insolvency resolution process under the Insolvency and Bankruptcy Code, 2016 (31 of 2016).

(2) The Central Government may make rules consistent with the provisions of this Act to ensure timely transfer of all matters, proceedings or cases pending before the Company Law Board or the courts, to the Tribunal under this section.

Lecture-XXVI

SPECIAL COURTS (Sections 435 to 446)

Establishment of Special Courts (Sec.435): [(1) The Central Government may, for the purpose of providing speedy trial of offences under this Act, by notification, establish or designate as many Special Courts as may be necessary.

(2) A Special Court shall consist of—

(a) a single judge holding office as Session Judge or Additional Session Judge, in case of offences punishable under this Act with imprisonment of two years or more; and

(b) a Metropolitan Magistrate or a Judicial Magistrate of the First Class, in the case of other offences,

who shall be appointed by the Central Government with the concurrence of the Chief Justice of the High Court within whose jurisdiction the judge to be appointed is working.]

Offences triable by Special Courts (Sec.436): (*1*) Notwithstanding anything contained in the Code of Criminal Procedure, 1973 (2 of 1974):

(*a*) all offences specified under sub-section (1) of Section 435 shall be triable only by the Special Court established for the area in which the registered office of the company in relation to which the offence is committed or where there are more Special Courts than one for such area, by such one of them as may be specified in this behalf by the High Court concerned;

(*b*) where a person accused of, or suspected of the commission of, an offence under this Act is forwarded to a Magistrate under sub-section (*2*) or sub-section (*2A*) of Section 167 of the Code of Criminal Procedure, 1973 (2 of 1974), such Magistrate may authorise the detention of such person in such custody as he thinks fit for a period not exceeding fifteen days in the whole where such Magistrate is a Judicial Magistrate and seven days in the whole where such Magistrate is an Executive Magistrate:

Provided that where such Magistrate considers that the detention of such person upon or before the expiry of the period of detention is unnecessary, he shall order such person to be forwarded to the Special Court having jurisdiction;

(*c*) the Special Court may exercise, in relation to the person forwarded to it under clause (*b*), the same power which a Magistrate having jurisdiction to try a case may exercise under section 167 of the Code of Criminal Procedure, 1973 (2 of 1974) in relation to an accused person who has been forwarded to him under that section; and

(*d*) a Special Court may, upon perusal of the police report of the facts constituting an offence under this Act or upon a complaint in that behalf, take cognizance of that offence without the accused being committed to it for trial.

(*2*) When trying an offence under this Act, a Special Court may also try an offence other than an offence under this Act with which the accused may, under the Code of Criminal Procedure, 1973 (2 of 1974) be charged at the same trial.

(*3*) Notwithstanding anything contained in the Code of Criminal Procedure, 1973 (2 of 1974), the Special Court may, if it thinks fit, try in a summary way any offence under this Act which is punishable with imprisonment for a term not exceeding three years:

Provided that in the case of any conviction in a summary trial, no sentence of imprisonment for a term exceeding one year shall be passed:

Provided further that when at the commencement of, or in the course of, a summary trial, it appears to the Special Court that the nature of the case is such that the sentence of imprisonment for a term exceeding one year may have to be passed or that it is, for any other reason, undesirable to try the case summarily, the Special Court shall, after hearing the parties, record an order to that effect and thereafter recall any witnesses who may have been examined and proceed to hear or rehear the case in accordance with the procedure for the regular trial.

Appeal and Revision (Sec.437): The High Court may exercise, so far as may be applicable, all the powers conferred by Chapters XXIX and XXX of the Code of Criminal Procedure, 1973 (2 of 1974) on a High Court, as if a Special Court within the local limits of the jurisdiction of the High Court were a Court of Session trying cases within the local limits of the jurisdiction of the High Court.

Application of Code of proceedings before Special Court (Sec.438): Save as otherwise provided in this Act, the provisions of the Code of Criminal Procedure, 1973 (2 of 1974) shall apply to the proceedings before a Special Court and for the purposes of the said provisions, the Special Court shall be [deemed to be a Court of Session or the court of Metropolitan Magistrate or a Judicial Magistrate of the First Class, as the case may be] and the person conducting a prosecution before a Special Court shall be deemed to be a Public Prosecutor.

Offences to be non-cognizable (Sec.439): (*1*) Notwithstanding anything in the Code of Criminal Procedure, 1973 (2 of 1974), every offence under this Act except the offences referred to in sub-section (*6*) of section 212 shall be deemed to be non-cognizable within the meaning of the said Code.

(*2*) No court shall take cognizance of any offence under this Act which is alleged to have been committed by any company or any officer thereof, except on the complaint in writing of the Registrar, a shareholder [or a member] of the company, or of a person authorised by the Central Government in that behalf:

Provided that the court may take cognizance of offences relating to issue and transfer of securities and non-payment of dividend, on a complaint in writing, by a person authorised by the Securities and Exchange Board of India:

Provided further that nothing in this sub-section shall apply to a prosecution by a company of any of its officers.

(*3*) Notwithstanding anything contained in the Code of Criminal Procedure, 1973 (2 of 1974), where the complainant under sub-section (*2*) is the Registrar or a person authorised by the Central Government, the presence of such officer before the Court trying

the offences shall not be necessary unless the court requires his personal attendance at the trial.

(*4*) The provisions of sub-section (*2*) shall not apply to any action taken by the liquidator of a company in respect of any offence alleged to have been committed in respect of any of the matters in Chapter XX or in any other provision of this Act relating to winding up of companies.

Explanation: The liquidator of a company shall not be deemed to be an officer of the company within the meaning of sub-section (*2*).

Transitional provisions (Sec.440): Any offence committed under this Act, which is triable by a Special Court shall, until a Special Court is established, be tried by a [Court of Session or the Court of Metropolitan Magistrate or a Judicial Magistrate of the First Class, as the case may be] exercising jurisdiction over the area, notwithstanding anything contained in the Code of Criminal Procedure, 1973 (2 of 1974):

Provided that nothing contained in this section shall affect the powers of the High Court under section 407 of the Code to transfer any case or class of cases taken cognizance by a [Court of Session or the Court of Metropolitan Magistrate or a Judicial Magistrate of the First Class, as the case may be] under this section.

Compounding of certain offences (Sec.441): (*1*) Notwithstanding anything contained in the Code of Criminal Procedure, 1973 (2 of 1974), any offence punishable under this Act (whether committed by a company or any officer thereof) [not being an offence punishable with imprisonment only, or punishable with imprisonment and also with fine], may, either before or after the institution of any prosecution, be compounded by:

(*a*) the Tribunal; or

(*b*) where the maximum amount of fine which may be imposed for such offence does not exceed twenty five lakh rupees, by the Regional Director or any officer authorised by the Central Government,

on payment or credit, by the company or, as the case may be, the officer, to the Central Government of such sum as that Tribunal or the Regional Director or any officer authorised by the Central Government, as the case may be, may specify:

Provided that the sum so specified shall not, in any case, exceed the maximum amount of the fine which may be imposed for the offence so compounded:

Provided further that in specifying the sum required to be paid or credited for the compounding of an offence under this sub-section, the sum, if any, paid by way of additional fee under sub-section (2) of section 403 shall be taken into account:

Provided also that any offence covered under this sub-section by any company or its officer shall not be compounded if the investigation against such company has been initiated or is pending under this Act.

(2) Nothing in sub-section (1) shall apply to an offence committed by a company or its officer within a period of three years from the date on which a similar offence committed by it or him was compounded under this section.

Explanation: For the purposes of this section:

(a) any second or subsequent offence committed after the expiry of a period of three years from the date on which the offence was previously compounded, shall be deemed to be a first offence;

(b) "Regional Director" means a person appointed by the Central Government as a Regional Director for the purposes of this Act.

(3) (a) Every application for the compounding of an offence shall be made to the Registrar who shall forward the same, together with his comments thereon, to the Tribunal or the Regional Director or any officer authorised by the Central Government, as the case may be.

(b) Where any offence is compounded under this section, whether before or after the institution of any prosecution, an intimation thereof shall be given by the company to the Registrar within seven days from the date on which the offence is so compounded.

(*c*) Where any offence is compounded before the institution of any prosecution, no prosecution shall be instituted in relation to such offence, either by the Registrar or by any shareholder of the company or by any person authorised by the Central Government against the offender in relation to whom the offence is so compounded.

(*d*) Where the compounding of any offence is made after the institution of any prosecution, such compounding shall be brought by the Registrar in writing, to the notice of the court in which the prosecution is pending and on such notice of the compounding of the offence being given, the company or its officer in relation to whom the offence is so compounded shall be discharged.

(*4*) The Tribunal or the Regional Director or any officer authorised by the Central Government, as the case may be, while dealing with a proposal for the compounding of an offence for a default in compliance with any provision of this Act which requires a company or its officer to file or register with, or deliver or send to, the Registrar any return, account or other document, may direct, by an order, if it or he thinks fit to do so, any officer or other employee of the company to file or register with, or on payment of the fee, and the additional fee, required to be paid under section 403, such return, account or other document within such time as may be specified in the order.

(*5*) Any officer or other employee of the company who fails to comply with any order made by the Tribunal or the Regional Director or any officer authorised by the Central Government under sub-section (*4*) shall be punishable with imprisonment for a term which may extend to six months, or with fine not exceeding one lakh rupees, or with both.

(*6*) Notwithstanding anything contained in the Code of Criminal Procedure, 1973 (2 of 1974), any offence which is punishable under this Act with imprisonment only or with imprisonment and also with fine shall not be compoundable.

(*7*) No offence specified in this section shall be compounded except under and in accordance with the provisions of this section.

Mediation and Conciliation Panel (Sec.442): (*1*) The Central Government shall maintain a panel of experts to be called as the Mediation and Conciliation Panel consisting of such number of experts having such qualifications as may be prescribed for mediation between the parties during the pendency of any proceedings before the Central Government or the Tribunal or the Appellate Tribunal under this Act.

(*2*) Any of the parties to the proceedings may, at any time during the proceedings before the Central Government or the Tribunal or the Appellate Tribunal, apply to the Central Government or the Tribunal or the Appellate Tribunal, as the case may be, in such form along with such fees as may be prescribed, for referring the matter pertaining to such proceedings to the Mediation and Conciliation Panel and the Central Government or Tribunal or the Appellate Tribunal, as the case may be, shall appoint one or more experts from the panel referred to in sub-section (*1*).

(*3*) The Central Government or the Tribunal or the Appellate Tribunal before which any proceeding is pending may, *suo motu*, refer any matter pertaining to such proceeding to such number of experts from the Mediation and Conciliation Panel as the Central Government or the Tribunal or the Appellate Tribunal, as the case may be, deems fit.

(*4*) The fee and other terms and conditions of experts of the Mediation and Conciliation Panel shall be such as may be prescribed.

(*5*) The Mediation and Conciliation Panel shall follow such procedure as may be prescribed and dispose of the matter referred to it within a period of three months from the date of such reference and forward its recommendations to the Central Government or the Tribunal or the Appellate Tribunal, as the case may be.

(*6*) Any party aggreived by the recommendation of the Mediation and Conciliation Panel may file objections to the Central Government or the Tribunal or the Appellate Tribunal, as the case may be.

Power of Central Government to appoint company prosecutors (Sec.443): Notwithstanding anything contained in the Code of Criminal Procedure, 1973 (2 of 1974), the Central Government may appoint generally, or for any case, or in any case, or for any specified class of cases in any local area, one or more persons,

as company prosecutors for the conduct of prosecutions arising out of this Act and the persons so appointed as company prosecutors shall have all the powers and privileges conferred by the Code on Public Prosecutors appointed under section 24 of the Code.

Appeal against acquittal (Sec.444): Notwithstanding anything contained in the Code of Criminal Procedure, 1973 (2 of 1974), the Central Government may, in any case arising under this Act, direct any company prosecutor or authorise any other person either by name or by virtue of his office, to present an appeal from an order of acquittal passed by any court, other than a High Court, and an appeal presented by such prosecutor or other person shall be deemed to have been validly presented to the appellate court.

Compensation for accusation without reasonable cause (Sec.445): The provisions of section 250 of the Code of Criminal Procedure, 1973 (2 of 1974) shall apply *mutatis mutandis* to compensation for accusation without reasonable cause before the Special Court or the Court of Session.

Application of fines (Sec.446): The court imposing any fine under this Act may direct that the whole or any part thereof shall be applied in or towards payment of the costs of the proceedings, or in or towards the payment of a reward to the person on whose information the proceedings were instituted.

Factors for determining level of punishment: 446A: The court or the Special Court, while deciding the amount of fine or imprisonment under this Act, shall have due regard to the following factors, namely:- (a) size of the company; (b) nature of business carried on by the company; (c) injury to public interest; (d) nature of the default; and (e) repetition of the default.

Lesser penalties for One Person Companies or small companies: 446B: Notwithstanding anything contained in this Act, if a One Person Company or a small company fails to comply with the provisions of sub-section (5) of section 92, sub-section (2) of section 117 or sub-section (3) of section 137, such company and officer in default of such company shall be liable to a penalty which shall not be more than one half of the penalty specified in such sections.